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IN THE

Supreme Court of the United States

October Term, 1944.

No. 220

Canadian River Gas Company, a Corporation, *Petitioner*

v.

Federal Power Commission, City and County of Denver, Colorado, Public Service Commission of Wyoming, Cheyenne Light, Fuel & Power Company, Public Service Company of Colorado, and Colorado Interstate Gas Company, *Respondents*.

BRIEF OF THE INDEPENDENT NATURAL GAS ASSOCIATION OF AMERICA, AMICUS CURIAE.

Carl L. Wheat,
Robert E. May,
520 Shoreham Building,
Washington, D. C.
Attorneys.

January 8, 1945.

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(*Note:* Unless otherwise indicated, all emphasis has been supplied by the authors of this brief.)

IN THE

Supreme Court of the United States

OCTOBER TERM, 1944.

No. 380.

CANADIAN RIVER GAS COMPANY, a Corporation, *Petitioner*

v.

FEDERAL POWER COMMISSION, CITY AND COUNTY OF DENVER, COLORADO, PUBLIC SERVICE COMMISSION OF WYOMING, COLORADO-WYOMING GAS COMPANY, PUBLIC SERVICE COMPANY OF COLORADO, AND COLORADO INTERSTATE GAS COMPANY, *Respondents.*

BRIEF OF THE INDEPENDENT NATURAL GAS ASSOCIATION OF AMERICA, AMICUS CURIAE.

This brief of the Independent Natural Gas Association of America is presented *amicus curiae*, under Rule 27, paragraph 9, of the Rules of this court.

OPINIONS BELOW.

The opinion of the Circuit Court of Appeals for the Tenth Circuit in this proceeding is reported in 142 F. (2d) 943. The opinion and order of the Federal Power Commission is reported in 43 P.U.R. (N.S.) 205.

JURISDICTION.

Jurisdiction of this Court is invoked by the Petitioner under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925, and Section 19(b) of the Natural Gas Act. (Pet. for Cert., p. 2).

PRELIMINARY STATEMENT.

The Independent Natural Gas Association of America is a corporation organized and existing under the laws of the state of Delaware. The membership of the Association consists of persons and corporations engaged in the production, gathering, transportation and sale of natural gas, and includes a number of royalty owners. Under the Association's charter, one of its principal purposes is to "promote and advance the welfare, progress and development of the natural gas industry in the United States of America and particularly to protect the interests of the producers of natural gas." In respect to regulation of the production and gathering of natural gas, the Board of Directors of the Association, at a meeting held in Tulsa, Oklahoma, on August 1, 1944, adopted the following resolution:

> "Resolved, That it is the definite opinion of the Independent Natural Gas Association of America that the regulation of the production, gathering and conservation of natural gas is the function of the respective producing states, and not of any Federal agency."

The Association, accordingly, has a direct and immediate interest in the instant proceeding, especially in respect to the question whether the Federal Power Commission exceeded the jurisdiction vested in it by the Natural Gas Act when it asserted and exercised authority over the production and gathering facilities of the Canadian River Gas Company. The precedent to be established in this case is of great significance and importance to the natural gas industry as a whole.

STATEMENT OF THE CASE.

This proceeding involves the validity of an order of the Federal Power Commission (hereinafter referred to as the Commission), adopted on March 18, 1942, reducing rates for the transportation and sale of natural gas by the Canadian River Gas Company (hereinafter referred to as Canadian). Canadian obtained a review of this order of the Commission by the United States Circuit Court of Appeals for the Tenth Circuit. That Court affirmed the order of the Commission in a judgment entered on July 8, 1944. A petition for Certiorari was filed with this Court by Canadian on August 22, 1944. On November 13, 1944, this Court granted said petition, but limited its review to Question No. 8, relating to the validity of the Commission's action in respect to the separation or allocation of properties. Canadian filed a petition for rehearing and enlargement of the scope of review on December 4, 1944, and this Court, by order entered on January 2, 1945, broadened the scope of review to include Questions Nos. 1, 2, and 3. Question No. 1, in which the Independent Natural Gas Association of America is particularly interested, reads as follows:

> "1. Whether the Circuit Court, after correctly holding that the Commission has no rate regulatory jurisdiction over Canadian's production and gathering properties, facilities and business, erroneously concluded and ruled that the Commission in this case did not exercise such prohibited jurisdiction."

Canadian is engaged in the production, gathering, transportation and sale of natural gas. Natural gas is produced from its leaseholds in the Panhandle (Texas) Gas Field. A portion of the gas so produced goes into Canadian's gathering or field system which terminates at Bivins Station, Texas. After compression at Bivins Station, the gas is transported, for a distance of approximately 86 miles through a main 22 inch transmission line to Clayton Junction, New

Mexico, where it is sold and delivered to the Colorado Interstate Gas Company for ultimate consumption in the State of Colorado. The remainer of the gathered gas produced by Canadian in the Panhandle Gas Field goes into Canadian's gathering or field system which terminates at Fritch Station, in Texas. After compression at Fritch Station, the gas is then transported by Canadian, through facilities leased from Texoma Natural Gas Company, to Gray Junction, Oklahoma, where the gas is sold to the Colorado Interstate Gas Company. (R., V. 1, p. 143). Canadian also sells gas to the Amarillo Oil Company, at the wells in the field, for ultimate distribution in the cities of Amarillo and Channing, Texas, and along the route of its pipeline for ultimate distribution in Dellart, Hartley and Texline, Texas, and in Clayton, New Mexico (R., V. 2, p. 708).

It is an established fact, which was clearly recognized by the Commission in its opinion in this proceeding, that Canadian's operations may readily be classified as between the production, the gathering, the transportation and the sale of natural gas. Nevertheless, the Commission made no distinction between these different functions performed by Canadian. Instead, the Commission grouped all of the functions together, and, for the purpose of its rate reduction order, determined rate base, revenues, expenses and rate of return on all of Canadian's operations, on the premise that production and gathering constituted an "integral" part of Canadian's operations and therefore should be treated in the same manner as facilities used for the transportation and sale of natural gas in interstate commerce (R., Vol. 1, p. 143, 146).

STATUTE INVOLVED.

The pertinent provisions of the Natural Gas Act (52 Stat. 821; 15 U.S.C. 717) are printed in Appendix A of this brief.

QUESTION PRESENTED.

The primary question to be argued in this brief is Question No. 1 of Canadian's petition for a writ of certiorari herein, namely, whether the Circuit Court of Appeals, after correctly holding that the Commission has no rate regulatory jurisdiction over Canadian's production and gathering properties, facilities and business, erroneously concluded and ruled that the Commission in this case did not exercise such prohibited jurisdiction. Incidental to this question, we will consider the adverse effect of the exercise of jurisdiction by the Commission over production and gathering upon the field operations of companies engaged in the natural gas business.

ARGUMENT.

I. Production and Gathering of Natural Gas Are Specifically Exempted from the Jurisdiction of the Commission Under the Provisions of the Natural Gas Act

When Congress enacted the Natural Gas Act of June 21, 1938 (52 Stat. 821, 15 U.S.C. 717), it did not vest the Federal Power Commission with full and complete jurisdiction over the natural gas industry. On the contrary, limitations upon the jurisdiction of the Commission were specifically set forth in the very first section of the Act, which reads as follows:

> "(a) As disclosed in reports of the Federal Trade Commission made pursuant to S. Res. 83 (Seventieth Congress, first session) and other reports made pursuant to the authority of Congress, it is hereby declared that the business of transporting and selling natural gas for ultimate distribution to the public is affected with a public interest, and that Federal regulation in matters relating to the transportation of natural gas and the sale thereof in interstate and foreign commerce is necessary in the public interest.
>
> "(b) The provisions of this Act shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for

resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale, *but shall not apply* to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or *to the production or gathering of natural gas.*"

It is obvious that the provisions of the Act were thus made applicable only to the *transportation* of natural gas in interstate commerce and to the *sale* in interstate commerce of natural gas for *resale* for ultimate public consumption. The provisions of the Act specifically do *not* apply (1) to any other transportation or sale of natural gas, (2) to the local distribution of natural gas or to the facilities used for such distribution or (3) to the production or gathering of natural gas. No language could possibly be plainer as to the limitations which Congress desired to place and did place, upon the Commission's authority under the Natural Gas Act.

When it enacted that statute, therefore, Congress was careful to confine and limit the jurisdiction of the Commission to the particular transportation or sale of natural gas intended to be covered by the provisions of the Act. Production and gathering were explicitly excluded.

Sec. 2(6) defines a "natural-gas company" to mean "a person engaged in the transportation of natural gas in interstate commerce, or the sale in interstate commerce of such gas for resale." Sec. 4 and 5(a), which are the rate regulatory provisions of the Act, refer to charges for the "transportation or sale of natural gas subject to the jurisdiction of the Commission." Sec. 7(a) relates to the extension or improvement of "transportation" facilities. Sec. 7(b) refers to the abondonment of "facilities subject to the jurisdiction of the Commission." Sec. 7(c)[1] covers the construction or extension of facilities for "the transporta-

[1]This section was amended by the Act of February 7, 1942, c. 49 (56 Stat. 83).

tion or sale of natural gas, subject to the jurisdiction of the Commission."

Aside from its use in the exemption provision in Sec. 1(b), the word "production" appears only in Sec. 5(b), 9(a), 10(a) and 11(a) of the Act. Sec. 5(b) provides that the Commission, upon its own motion, or upon the request of any State commission, whenever it can do so without prejudice to the efficient and proper conduct of its affairs "may investigate and determine the cost of the production or transportation of natural gas by a natural-gas company in cases where the Commission has no authority to establish a rate governing the transportation or sale of such natural gas." This provision obviously has for its sole purpose the aiding of State regulation, and vests no authority in the Commission to exercise direct jurisdiction over the production activities of a natural-gas company. As a matter of fact, the legislative history of this subsection fully corroborates the view that Congress did not intend to give the Commission any such direct jurisdiction over the production activities of a natural gas company.[1] The Commission

[1]Commenting upon this section in its report on the legislation, the House Committee stated that it "will greatly aid State commissions in their rate-making proceedings." (H. Rep. No. 709, 75th Cong., 1st Sess. on H. R. 6586). This subsection, in the form in which it appeared in H. R. 4008 (75th Cong., 1st Sess.), did not contain the limiting language "by a natural-gas company." Objection thereto was registered by Congressman Boren of Oklahoma and Chairman Maltbie of the New York Public Service Commission on the ground that the subsection constituted an extension of authority into the State field (Hearings on H. R. 4008, 75th Congress, 1st Sess., pages 46, 106-110, 147). When the bill reached the House for debate, Congressman Boren offered an amendment, which was adopted, inserting the qualifying words "by a natural-gas company." Congressman Boren stated that it was the purpose of the amendment "to keep the jurisdiction of the Federal Government as clearly defined as possible from the jurisdiction of the State government in cases arising under the provisions of the bill" and that the amendment "assures us that the Federal Government will not go into a realm where the State government already has proper authority to handle the problem." (Cong. Rec. 75th Cong., 1st Sess., Vol. 81, Part 6, page 6728).

has itself construed this provision as designed to aid State and local regulation. *Re The East Ohio Gas Company*, 28 P.U.R. (N.S.) 129; 115 F. (2d) 385.

Sec. 9(a) of the Act authorizes the Commission to determine, and by order fix, proper and adequate rates of depreciation and amortization in respect to the several classes of property of each natural-gas company used or useful in the "production, transportation, or sale of natural gas." This section, however, contains a proviso to the effect that

> "Nothing in this section shall limit the power of a State commission to determine in the exercise of its jurisdiction, with respect to any natural-gas company, the percentage rates of depreciation or amortization to be allowed, as to any class of property of such natural-gas company, or the composite depreciation or amortization rate, for the purpose of determining rates or charges."

In other words, what Congress did in sec. 9(a) of the Act was to vest the Commission with jurisdiction to determine depreciation and amortization rates of natural-gas companies, but at the same time it expressily recognized the right of State authorities to determine such depreciation and amortization rates, even in respect to a "natural-gas company" (defined in the Act to be a person engaged in the transportation of natural gas in interstate commerce, or the sale in interstate commerce of such gas for resale). This is another example of the scrupulous care which Congress exercised, when it enacted the Natural Gas Act, not in any way to interfere with the authority of the States in the respects in which they were considered authorized to act, even when interstate commerce might be involved, namely, in the fields of distribution, production, and gathering of natural gas.

In any event, the mention of "production" in Sec. 9(a) in respect to the determination of depreciation and amortization charges, may not properly be used as a predicate for

the assertion of jurisdiction by the Commission over the production of natural gas, in the manner in which it exercised such jurisdiction in the proceeding under review. Determination and prescription of depreciation and amortization charges are primarily accounting problems, and may be considered separate and apart from the fixation of just and reasonable rates to be charged for public utility or transportation services. *Northwestern Bell Telephone Company* v. *Nebraska State Railway Commission*, 297 U.S. 471; *American Telephone and Telegraph Company* v. *United States*, 299 U.S. 232. Thus, under a statutory provision analogous to Section 9(a) of the Natural Gas Act, namely, Section 20(5) of the Interstate Commerce Act (41 Stat. 493), the Interstate Commerce Commission considered the determination and prescription of depreciation charges for telephone companies without regard to the use thereof in rate proceedings. *Depreciation Charges for Telephone Companies*, 177 I.C.C. 351.

Section 10(a) of the Act authorizes the Commission to require natural-gas companies to file periodic or special reports, including, among other things, "full information as to assets and liabilities, capitalization, investment and reduction thereof, gross receipts, interest due and paid, depreciation, amortization, and other reserves, cost of facilities, cost of maintenance and operation of facilities for the *production*, transportation, or sale of natural gas, cost of renewal and replacement of such facilities, transportation, delivery, use, and sale of natural gas." The mere inclusion in this subsection of the power to require information in respect to facilities used in the "production" of natural gas (when such "production" was specifically excluded from the Commission's jurisdiction by Section 1(b), obviously cannot be deemed in any manner to vest the Commission with a jurisdiction over production activities which has already been specifically excluded. This Court has repeatedly held that a regulatory body may require information from a regulated company with respect to all of its operations, even

though a portion of such operations may not be subject to regulation by the tribunal requiring the information. *Arkansas Louisiana Gas Company* v. *Department of Public Utilities*, 304 U.S. 61; *Natural Gas Pipeline Company of America* v. *Slattery*, 302 U.S. 300; *Interstate Commerce Commission* v. *Goodrich Transit Company*, 224 U.S. 194. In the last cited case, the court declared:

> "It is a mistake to suppose that the requiring of information concerning the business methods of such corporations, as shown in its accounts, is a regulation of business not within the jurisdiction of the Commission, as seems to be argued. The object of requiring such accounts to be kept in a uniform way, and to be open to the inspection of the Commission, is *not to enable it to regulate the affairs of the corporations not within its jurisdiction*, but to be informed concerning the business methods of the corporations subject to the act, that it may properly regulate such matters as are really within its jurisdiction."

In Section 11(a) of the Natural Gas Act it is provided that in case two or more states propose to the Congress compacts dealing with the "conservation, production, transportation, or distribution of natural gas," it shall be the duty of the Commission to assemble pertinent information relative thereto, to make public and to report to the Congress information so obtained, together with such recommendations for further legislation as may appear to be appropriate or necessary to carry out the purposes of such compact and to aid in the conservation of natural gas resources within the United States and in the orderly, equitable, and economic production, transportation, and distribution of natural gas.

It is obvious that Section 11(a) vests in the Commission no jurisdiction over the production of natural gas other than the power to investigate state compacts, to report them to Congress, and to make recommendations for further legislation. By no stretch of the imagination could this subsection

be construed as vesting in the Commission any power over production of natural gas such as was essayed to be exercised in the instant proceeding. This Court, in *Federal Power Commission* v. *Hope Natural Gas Company*, 320 U.S. 591, 613, commented that, by Section 11(a) of the Act, "Congress recognized the legitimate interests of the states in the conservation of natural gas," and added that "Congress was quite aware of the interests of the producing states in their natural gas supplies."

The only other provision of the Natural Gas Act which could in any manner be relied upon to support a contention that the Commission has any authority of any nature over production is Section 14(b), wherein it is provided that the Commission may, after hearing, "determine the adequacy or inadequacy of the gas reserves held or controlled by any natural-gas company, or by anyone on its behalf, including its owned or leased properties or royalty contracts" and that it may also, after hearing, "determine the propriety and reasonableness of the inclusion in operating expenses, capital, or surplus of all delay rentals or other forms of rental or compensation for unoperated lands and leases." The subsection further provides that the Commission, for the purpose of such determination, "may require any natural-gas company to file with the Commission true copies of all its lease and royalty agreements with respect to such gas reserves."

This provision appears in the section of the Act authorizing "investigations" by the Commission, and has no direct application to rate proceedings. Although the subjects covered in this subsection of the Act relate to certain of the field operations of natural-gas companies, it does not follow that Congress, by giving the Commission the power to "investigate" and "determine" such matters intended to expand the jurisdiction of the Commission to include regulation of production and gathering, in relation to rate fixation, and thereby repudiate and nullify the specific and un-

ambiguous exemption language contained in Section 1(b). It is entirely possible for the Commission, in its administration of the Act, to give full effect to the Congressional purpose, as expressed in Section 14(b), without regulating or attempting to regulate the production and gathering of natural gas as it has done in this proceeding. Concededly, the adequacy of the gas reserves available to a natural gas company may be an important factor to be considered in determining the general question of public convenience and necessity involved in the construction, extension or abadonment of facilities or service under Section 7 of the Act. *Re Kansas Pipeline and Gas Company*, 30 P.U.R. (N.S.) 321, 332; *Re Cabot Gas Corporation*, 43 P.U.R. (N.S.) 182, 47 P.U.R. (N.S.) 65, 51 P.U.R. (N.S.) 458. The amount of gas reserves available is also pertinent to the determination of amortization rates under Sec 9(a). Also, the question whether delay rentals should be properly chargeable to operating expense or capital is entirely relevant to a determination of correct accounting pursuant to the authority vested in the Commission in Section 8(a) of the Act to prescribe a system of accounts to be kept by natural-gas companies. The Commission prescribed such a system of accounts, effective January 1, 1940, and provided therein for a special treatment of exploration and development costs, including delay rentals, in the income accounts (Accounts 510-513).

It is apparent from the foregoing review, that neither the provisions of the Act which mention the word "production," nor the provision with respect to gas reserves and delay rentals, may properly be cited or used to sustain an assertion of jurisdiction by the Commission over production and gathering operations in a rate regulatory proceeding such as the instant case. It seems evident that Congress intended to exclude entirely from the Commission's rate jurisdiction "the production and gathering of natural gas," for it excluded such operations by language contained in the same subsection of the Act wherein it specifically defined the

Commission's jurisdiction as covering only the transportation and sale for resale of natural gas in interstate commerce. The language is clear and unequivocal. And the rate regulatory provisions of the Act followed the same pattern, namely, the Commission's jurisdiction was limited to the transportation and sale for resale of natural gas in interstate commerce.

The legislative history of the Natural Gas Act[1] also bears out and fully supports the position that Congress did not intend to vest in the Commission any authority over the production or gathering of natural gas, whether in rate proceedings or otherwise. In its report on the bill which became the Natural Gas Act, the House Committee on Interstate and Foreign Commerce (H. Rep. No. 709, 75th

[1] That the Congress intended to consider the problems peculiarly and particularly incident to regulation of the transportation and sale of natural gas, as a separate and distinct proposition, from regulation of the electric industry, is apparent from the legislative history of the Natural Gas Act. The Federal Trade Commission had made reports on its investigation of electric and gas utilities pursuant to Congressional authorization (Document 92, Parts 72-A and 73-A, 70th Cong., 1st Sess.). Federal regulation of the transportation and sale of natural gas was at first provided for in Title III of the bills (S. 1725 and H. R. 5423, 74th Cong., 1st Sess.) which eventually became the Public Utility Act of 1935 (49 Stat. 803). However, after hearings before the Congressional committees, the provisions relating to the regulation of natural gas were omitted from the bills reported by the Congressional committees (S. 2796, Senate Report No. 621 and H. R. 5423, House Report No. 1318, 74th Cong., 1st Sess.) and S. 2796, which became the Public Utility Act of 1935, did not contain provisions for the regulation of the transportation and sale of natural gas. The Federal Trade Commission submitted its final report on natural gas in December 1935 (Document 92, Part 84-A, 70th Cong., 1st Sess.). Various bills were thereafter introduced to regulate natural gas (S. 4180, H. R. 11662 and H. R. 12680, 74th Cong., 2nd Sess.; S. 1919, H. R. 4008, H. R. 5711 and H. R. 6586, 75th Cong., 1st Sess.). The only bills upon which Congressional hearings were held were H. R. 11662 (74th Cong., 2nd Sess.) and H. R. 4008 (75th Cong., 1st Sess.). H. R. 6586, 75th Cong., 1st Session, became the Natural Gas Act of 1938 (52 Stat. 821).

Cong., 1st Sess.) stated the general purpose of the legislation as follows:

"If enacted, the present bill would for the first time provide for the regulation of natural-gas companies transporting and selling natural gas in interstate commerce. It confers jurisdiction upon the Federal Power Commission over the transportation of natural gas in interstate commerce, and the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use. The States have, of course, for many years regulated sales of natural gas to consumers in intrastate transactions. The States have also been able to regulate sales to consumers even though such sales are in interstate commerce, such sales being considered local in character and in the absence of congressional prohibition subject to State regulation. (See *Pennsylvania Gas Co.* v. *Public Service Commission* (1920), 252 U. S. 23.) There is no intention in enacting the present legislation to disturb the States in their exercise of such jurisdiction. However, in the case of sales for resale, or so-called wholesale sales, in interstate commerce (for example, sales by producing companies to distributing companies) the legal situation is different. Such transactions have been considered to be not local in character and, even in the absence of Congressional action, not subject to State regulation. (See *Missouri* v. *Kansas Gas Company* (1924) 265 U. S. 298, and *Public Service Commission* v. *Attleboro Steam & Electric Co.* (1927) 273 U. S. 83.) The basic purpose of the present legislation is to occupy this field in which the Supreme Court has held that the States may not act.

"The bill takes no authority from State commissions, and is so drawn as to complement and in no manner usurp State regulatory authority, and contains provisions for cooperative action with State regulatory bodies.

"Your committee believes that this legislation is highly desirable to fill the gap in regulation that now exists by reason of the lack of authority of the State Commissions."

It will be noted that the House Committee specifically stated that the legislation was intended to be confined to the transportation and sale of natural gas in interstate commerce and to regulate sales for resale, or so-called wholesale sales, in interstate commerce, which were not subject to State regulation. The cases cited in the House Committee's report, namely, *Missouri v. Kansas Natural Gas Company*, 265 U. S. 298 and *Public Service Commission v. Attleboro Steam and Electric Company*, 273 U. S. 83, demonstrate the character of transaction which the legislation intended to regulate.

In the *Missouri case*, it appeared that the Kansas Natural Gas Company was transporting natural gas from points in the State of Oklahoma into the states of Kansas and Missouri and sold the gas at wholesale to independent distributing companies. The state commissions of Kansas and Missouri attempted to prescribe the rates to be charged by the Kansas Natural Gas Company to distributing companies in various cities and towns in the two states. The Court held the attempted regulation to be beyond the power of the state authorities, saying:

> "The business of supplying, on demand, local consumers is a local business, even though the gas be brought from another State and drawn for distribution directly from interstate mains; and this is so whether the local distribution be made by the transporting company or by independent distributing companies. In such case the local interest is paramount, and the interference with interstate commerce, if any, indirect and of minor importance. But here the sale of gas is in wholesale quantities, not to consumers, but to distributing companies for resale to consumers in numerous cities and communities in different States. The transportation, sale, and delivery constitute an unbroken chain, fundamentally interstate from beginning to end, and of such continuity as to amount to an established course of business. The paramount interest is not local but national; admitting of and requiring uniformity of regulation. Such uniformity, even though it be the

uniformity of governmental nonaction, may be highly necessary to preserve equality of opportunity and treatment among the various communities and States concerned."

In the *Attleboro case*, this Court dealt with an attempt on the part of the Rhode Island regulatory commission to fix the rate to be charged for electric energy generated in Rhode Island and transmitted and sold at the state line to a Massachusetts distributing company. This Court held the sale beyond the scope of state regulation.

The Commission, in its brief below in the instant cause, laid great stress upon the circumstance that the House Committee, in its report upon the proposed legislation, used as an example "sales by *producing* companies to distributing companies." We do not believe the use of this language is in any manner persuasive or controlling, especially in view of the fact that, if it is given the significance attached to it by the Commission, the specific exemption of "the production and gathering of natural gas" in Section 1 (b) of the Act would thereby be nullified. The all-embracing, unambiguous and unequivocal language of the statute should certainly be given greater weight than any such ambiguous phrase in the Committee report. Whereas the Committee, in this one reference, referred to sales by *producing* companies to distributing companies, the context of the preceding language in the report clearly demonstrates that only the transportation and sale for resale of natural gas were intended to be covered by the Act. It would be a most unusual (if not wholly unheard of) situation for a company only *producing* natural gas to make a sale in interstate commerce directly from its production property to a *distributing* company. Some *transportation* is obviously required from the field to the point of distribution to ultimate consumers.

Thus, it is obvious that the Natural Gas Act was intended by Congress to cover only the transportation and the sale of natural gas in interstate commerce for resale, or so-

called wholesale sales. It was specifically *not* intended to include the production, gathering, or local distribution of natural gas. The Congressional purpose was reiterated by Senator Wheeler, Chairman of the Senate Committee on Interstate Commerce, who sponsored the legislation in the Senate, when he engaged in the following colloquy with Senator Austin of Vermont during debate in the Senate (Cong. Rec., Vol. 81, Part 8, p. 9312):

> "Mr. Austin. Mr. President, may I ask the Senator from Montana a question concerning this bill? Does the bill undertake to regulate the production of natural gas, or does it undertake to regulate the producers of natural gas?
>
> "Mr. Wheeler. It does not attempt to regulate the production of natural gas or the distributors of natural gas; only those who sell it wholesale in interstate commerce."

It certainly was not the intention of the sponsors of the legislation to encompass production and gathering activities of natural gas companies within the scope of the Natural Gas Act. At a hearing on an earlier bill (Hearings on H. R. 11662, House Committee on Interstate and Foreign Commerce, 74th Cong., 2nd Sess., pages 17, 28) Mr. Dozier DeVane, then Solicitor of the Federal Power Commission, stated that:

> "Mr. DeVane. The bill makes no attempt to regulate the production or gathering facilities of a natural-gas company, this function being purely local in character. . . ."
>
> "Mr. DeVane. Now, section 1 (b) also provides that the Commission shall have no jurisdiction over the gathering or gathering rates for natural gas.
>
> "Mr. Cooper. What do you mean by gathering rates?
>
> "Mr. DeVane. The rates that are paid in the gathering field, Mr. Cooper.
>
> "Mr. Cooper. All right."

Chairman Lea of the House Committee on Interstate and Foreign Commerce, who sponsored the bill which became the Natural Gas Act, stated on the floor of the House, when he presented the legislation, that the "bill does not apply to the production and gathering of gas." (Cong. Rec., Vol. 81, Part 6, p. 6721).

It is thus apparent, from the legislative history of the Natural Gas Act, that Congress clearly intended to cover only the *transportation* and *sale* of natural gas in interstate commerce, and expressly excepted the *production*, *gathering* and *distribution* of natural gas. Congress was fully aware of the differences between the functional operations of natural gas companies, and with such full and complete knowledge, it expressly and in plain language excepted production and gathering.

II. The Commission Improperly Asserted Jurisdiction Over Production and Gathering in this Proceeding.

Notwithstanding the clear and unambiguous language of the statute and the legislative history thereof, the Commission has in this proceeding assumed jurisdiction over the production and gathering of natural gas by Canadian, and over its facilities used for such production and gathering. The purported justification for this assertion of jurisdiction is the statement in the Commission's opinion that Canadian's production and gathering operations are an integral part of its total operations, and that it is therefore "indispensable" for the Commission to investigate its production and gathering operations and property and to deal with the same in establishing the rate base, in order to regulate the Company's rates and charges for the sale of natural gas in interstate commerce for resale and for the transportation of natural gas in interstate commerce. The complete discussion of the Commission on this subject follows:

> "The particular contention of Canadian, that insofar as it is engaged in the production and gathering of natural gas it is not subject to the jurisdiction of the

Commission, is unsound. Canadian's production and gathering operations are an integral part of its total operations, including transportation in interstate commerce and the sale of natural gas for resale in interstate commerce. Furthermore, Canadian's operations are an integral part of Colorado's operations and the two comprise a single operating system. The investigation of Canadian's production and gathering property and operations is indispensable in regulating Canadian's rates and charges for the sale of natural gas in interstate commerce for resale and for the transportation of natural gas in interstate commerce."

The Commission made no reference whatever, in its discussion of this jurisdictional question, to the fact that, under Sec. 1 (b), the provisions of the Act are specifically made inapplicable to "the production or gathering of natural gas." In effect, the exemption of production and gathering from its jurisdiction was cast aside by the Commission on the premise that if the Commission should determine that it is necessary or "indispensable" to exercise such jurisdiction, then it may do so, irrespective of the clear and unequivocal language of the statute to the contrary.

The Circuit Court of Appeals recognized that, under the provisions of Sec. 1 (b) of the Act, Canadian River's production and gathering properties and facilities "lie beyond the range of the rate-regulatory jurisdiction of the Commission." However, the Circuit Court upheld the Commission's action on the ground that the Commission did not really exercise jurisdiction over production and gathering "as such," because the Commission did not separately prescribe rates or charges applicable to the company's production or gathering operations. The Court stated that the Commission's inquiry into production and gathering activities was "merely in their relation to the fixing of reasonable rates to be exacted and received for the natural gas moved in interstate commerce and sold for resale," and the Court stated that it failed "to find in the Act anything which expressly or by fair implication indicates a Congres-

sional purpose to restrict or withhold from the Commission jurisdiction in a case of this kind to take into consideration the production and gatherng properties only as they have bearing upon the question of the fixing of reasonable rates for gas moved interstate and sold for public consumption." The Court also stated that the Commission "did not attempt to affect in any manner the acquiring and maintaining of gas leaseholds, gas rights, or gas wells," nor "did it undertake to affect anywise the location, construction, extension or physical connections of pipelines, or the operation of pipelines or other facilities constituting the gathering properties." (142 F. (2d) 952-953.)

We submit that both the Commission and the Circuit Court wholly disregarded the unequivocal language of the statute, which excludes from the Commission's jurisdiction, without any exception whatsoever, "the production or gathering of natural gas." There is nothing in the language of the Act itself, nor in its legislative history, which either intimates or suggests that it was the intention of Congress to vest in the Commission the discretionary power to determine that it could exercise jurisdiction over production and gathering upon a finding that the assertion of such jurisdiction is in its opinion necessary or "indispensable" in order effectively to regulate the transportation and sale of natural gas in interstate commerce. If that had been the legislative purpose, Congress most assuredly would have made that intention known. Instead, Congress, without any qualification or exception, excluded from the provisions of the Act "the production or gathering of natural gas." We most earnestly suggest that Congress meant precisely what it said when it used that language, and we urge that it is no less than a plain distortion of the legislative intent to contend that Congress meant to vest the Commission with the power to determine when and whether it should exercise jurisdiction over production and gathering operations. Yet, it is clear from the language used by the Commission in its discussion of this issue in its opinion in this case that the Commission thus interprets the provisions of the Act.

If the Commission considers the provisions of the Act inadequate effectively to enable it to perform its function to regulate rates and charges for the transportation or sale for resale of natural gas in interstate commerce, then it would seem appropriate for the Commission to seek amendatory legislation from Congress, rather than thus to attempt to stretch the provisions of the Act to include jurisdiction over a subject so obviously not in contemplation by Congress when it enacted this statute. If there is believed to be any defect in the present statute in respect to the necessity for regulation of production and gathering operations, the responsibility therefor rests with Congress, the legislative body. It is not the responsibility of the Commission or of the Courts to attempt to cure any such alleged defect by interpreting the Act to give the Commission the character of jurisdiction which Congress plainly intended it should not possess.

It is not difficult to imagine instances in which it would seem wise or unwise, necessary or unnecessary, dispensable or indispensable for the Commission to exercise jurisdiction over production and gathering operations. For example, one company may operate only gas wells, selling its natural gas at the well-head; another company may operate its gas wells in conjunction with gathering facilities and make sales either at the well-head or from the gathering facilities, while another company may operate not only gas wells, but also gathering *and* transportation facilities and may make sales at the well-head, from the gathering facilities, from the transportation facilities, or any combination thereof. Companies producing or gathering gas may or may not be affiliated with other companies engaged either in the production, gathering or transportation of natural gas, and if affiliated, the extent of the affiliation may be minor or major.

Our contention is that Congress, by the exclusion language contained in Section 1(b), did not intend to leave with the Commission the discretionary authority to deter-

mine whether or not it could or should exercise rate regulatory jurisdiction over production and gathering of natural gas in any such particular instance. Congress unqualifiedly excepted production and gathering from the Commission's authority, and effect should be given to the plain language of the statute. Of course, questions may conceivably arise as to whether a particular line is a "gathering" or a "transportation" facility, and the Commission doubtless has the primary responsibility of determining that question of fact in order to reach a conclusion on the question of jurisdiction. However, when the Commission has determined, as it did in the proceeding under review, that a portion of a company's operations are production or gathering operations, it may not, without disregarding the plain language of the statute, exercise jurisdiction over such production or gathering operations merely on the ground that in its opinion it is "indispensable" to assert such jurisdiction in order effectively to regulate the transportation and sale for resale of natural gas in interstate commerce.

In this connection, it seems pertinent and important to note that regulation by the Commission of the production and gathering of natural gas has now progressed to the point where the exclusion language contained in Section 1(b) on that subject has practically been interpreted out of the Natural Gas Act. In the first major test case involving the Commission's authority over production and gathering, namely, *Re Columbian Fuel Corporation*, 35 P.U.R. (N.S.) 3, the Commission had instituted a proceeding, on its own motion, suspending the operation of certain increases in prices for natural gas sold by the Columbian Fuel Corporation to the Warfield Natural Gas Company. The Commission found that the Columbian Fuel Corporation produced and gathered natural gas in the State of Kentucky, which it sold to the Warfield Natural Gas Company, the point of delivery of the gas being at the termini of the Columbian Company's gathering lines or from a compressor station owned and operated by it. All of the facilities

of the Columbian Company were located in the State of Kentucky, and deliveries of the gas were made within that State. Warfield Natural Gas Company owned and operated a natural gas transmission system in the State of Kentucky which connected with transmission lines of the United Fuel Gas Company at the Kentucky-West Virginia state line and with the transmission lines of the Atlantic Seaboard Corporation in the State of Kentucky. In respect to the ultimate disposition of the natural gas sold by the Columbian Company to the Warfield Company, the Commission found as follows:

> "(6) A part of the natural gas sold by respondent is resold by the latter within the state of Kentucky. A large portion of the gas sold by respondent to Warfield is resold by the latter to United and is transmitted into the state of West Virginia. The gas is then resold by United for commercial and industrial uses without the state of Kentucky. From 40 to 50 per cent of the gas sold by respondent to Warfield is delivered by the latter to the Seaboard line from which the gas is sold and delivered in large quantities to local distributing companies in West Virginia and Maryland.
>
> "(7) There is a regular unbroken and uninterrupted transmission and a continuous flow of the natural gas sold by respondent to Warfield from the areas in Kentucky to destinations in other states and in the District of Columbia. Such transportation is intended to be and is being carried on as an established course of business." (35 P.U.R. (N.S.) 3, 5-6).

The Columbian Company contended, among other things, that even on the assumption that its sales of natural gas to the Warfield Company were "sales in interstate commerce," the provisions of the Act were not applicable to it, as its function was solely that of a producer and gatherer of natural gas. It also contended that the sales to the Warfield Company were not sales in interstate commerce and that it was therefore not a natural-gas company within the meaning of the provisions of the Act.

This proceeding provoked considerable interest, not only within the industry, but also on the part of state regulatory officials. *Amici curiae* included the Public Service Commission of West Virginia, the National Association of Railroad and Utilities Commissioners, the Mid-Continent Oil and Gas Association, and the Independent Petroleum Association of America. Briefs were filed on behalf of these organizations and their counsel participated in oral argument before the Commission. Uniformly, all of the *amici curiae* supported the Columbian Company's contention that the sales of natural gas involved were not subject to the Commission's jurisdiction under the provisions of the Natural Gas Act. The opposite contention was made by counsel for the Federal Power Commission, who filed a brief and participated in the oral argument before it, and who urged the Commission to assert jurisdiction.

The Commission (with one Commissioner alone dissenting) declined to assume jurisdiction over the sales involved in the *Columbian Fuel case*, vacated the order of suspension, and dismissed the proceeding. In reaching the conclusion that the Commission lacked jurisdiction in this particular case, the majority opinion of the Commission appears definitely to indicate that there was no question in the minds of the participating Commissioners but that the sales in question were *in interstate commerce*. The negative language in Section 1(b), excluding from the provisions of the Act "the production or gathering of natural gas," however, was held to be controlling and determinative of the jurisdictional issue. Accordingly, in that case, the Commission apparently determined that the Act does not vest it with jurisdiction over sales of natural gas in interstate commerce when such sales are merely incidental to the production and gathering of natural gas.

There is language in the opinion in the *Columbian Fuel case*, however, which might be interpreted as qualifying the general statement that the Commission held that it does not have jurisdiction over sales of natural gas in interstate

commerce which are thus merely incidental to production and gathering. The Commission concluded that "it was not the intention of Congress to subject to regulation under the Natural Gas Act *all* persons whose only sales of natural gas in interstate commerce, as in that case, are made as an incident to and immediately upon completion of such person's production and gathering of said natural gas and who are not otherwise subject to the jurisdiction of this Commission." The Commission then alluded to the circumstance that further experience with the administration of the Natural Gas Act "may reveal that the initial sales of large quantities of natural gas which eventually flows in interstate commerce are by producing or gathering companies which, *through affiliation, field agreement, or dominant position in a field*, are able to maintain an unreasonable price despite the appearance of competition." Under such circumstances, the Commission stated, it "will decide whether it can assume jurisdiction over arbitrary field prices under the present act or should report the facts to Congress with recommendations for such broadening of the act and provision of additional machinery as may appear necessary to close this gap in effective regulation of the natural gas industry." Apparently it did not occur to the Commission that it could deal effectively with such unusual cases, where unreasonable prices were being charged, through the exercise of its proper authority over the allowable operating expenses of the transportation entities, rather than by doing violence to the Act through disregard of the exemption of production and gathering activities from its jurisdiction. We shall discuss this phase of the problem briefly at a later point.

Apparently adhering to its ruling in the *Columbian Fuel case*, the Commission subsequently issued various orders exempting particular companies from the provisions of the Natural Gas Act. In these orders the Commission found that the companies involved were engaged only in the production and gathering of natural gas, that sales were made

either from the well mouth or at the end of the gathering facilities, that there was no affiliation between the selling and purchasing companies, and that the applicant companies did not occupy "dominant" positions in their respective fields which enabled them to control prices of production.[1]

However, since the decision of the United States Court of Appeals for the District of Columbia in *Peoples Natural Gas Company* v. *Federal Power Commission*, 127 F. (2d) 153 (cert. denied, 316 U. S. 700), the Commission has apparently adopted the position that it has all-inclusive jurisdiction over sales from production and gathering facilities, notwithstanding the language to the contrary in Section 1(b) of the Act. For example, in an opinion in a rate proceeding, *In the Matter of Interstate Natural Gas Company*, 48 P.U.R. (N.S.) 267, 273, the Commission, apparently disregarding the position which it had taken in the *Columbian Fuel case, supra*, commented as follows:

> "The negative language in Section 1(b) upon which the Interstate Company relies for its claimed exemption involving these sales provides that the Commission shall not have jurisdiction over 'the production or gathering of natural gas.' When the distinction between *production and gathering* of natural gas, and the *sale* of such gas in interstate commerce is kept in mind, effect is given to the Congressional objective. [Footnote: For the distinction between production of a commodity and sales of such commodity in interstate commerce, see *Carter* v. *Carter Coal Co.*, 298 U. S. 238, 302-4.] The Commission is bound to obey the command of Congress to regulate these sales in interstate commerce for resale to the three pipe line Companies. Such is clearly the implication of the decision of the

[1] See orders *In the Matter of Repollo Oil Company* (Docket No. G-195, July 1, 1941); *Sinclair Prairie Oil Company* (Docket No. G-197, July 8, 1941); *Kentucky Ohio Gas Company* (Docket No. G-198, July 8, 1941); *Magnolia Petroleum Company* (Docket No. G-189, July 8, 1941); *Sinclair Wyoming Oil Company* (Docket No. G-196, July 15, 1941); *The Chartiers Oil Company* (Docket No. G-191, September 9, 1941).

Circuit Court of Appeals in *Peoples Natural Gas Co.* v. *Federal Power Commission*, 127 F. (2d) 153; cert. den. 316 U. S. 700."

In their brief in the Circuit Court of Appeals for the Tenth Circuit in this proceeding, Counsel for the Commission relied strongly upon the decision of the Court of Appeals of the District of Columbia in the *Peoples case* there cited, to support their claim that the Commission had exercised proper authority over Canadian's production and gathering operations. We believe that a fair analysis of the decision in the *Peoples case* definitely discloses that it does not support the Commission's contention.

In the *People's case*, the Commission had instituted an investigation to determine whether the Company was a "natural-gas company," as defined in the Natural Gas Act, and also whether any of its rates, subject to the Commission's jurisdiction, were unjust or unreasonable. In connection with this investigation, the Commission sought access to certain of the Company's books and records, and upon failure of the Company to comply, the Commission brought an action in the District Court to compel compliance with its subpoenas requiring production of certain books and records. The District Court held with the Commission, and the case was appealed to the Court of Appeals for the District of Columbia. It is apparent that the decision of the Court of Appeals, which upheld the right of the Commission to subpoena the books and records, was predicated almost entirely upon a factual allegation by the Commission, which was not denied by the Peoples Company, that it made a sale of natural gas for resale in interstate commerce to an affiliated company. The Court said:

"The Commission's motion, apart from annexed exhibits, does not clearly allege any facts which show that the Commission had jurisdiction to demand these books and records. But in Paragraph IX the Commission annexed to and expressly made a part of its motion, as Exhibit F, a copy of an order by which it had di-

rected its counsel to bring the present proceedings. In Paragraph (d) of Exhibit F the Commission states: 'The testimony and evidence adduced (at a certain hearing) shows, among other things, that Peoples sells natural gas at its new compressor station in Clarion County, Pennsylvania, to New York State Natural Gas Corporation, an affiliated company, and that the latter immediately transports said natural gas into the State of New York where it sells the same to others for resale for ultimate public consumption * * *.'

"The sales thus described are sales in interstate commerce [citing *Public Utilities Commission of Rhode Island* v. *Attleboro Steam and Electric Company*, 273 U. S. 83; *Missouri* v. *Kansas Natural Gas Company*, 265 U. S. 298; *Illinois Natural Gas Company* v. *Central Illinois Public Service Company*, 314 U. S. 498; *United States* v. *Rock Royal Cooperative, Inc.*, 307 U. S. 533; *Currin* v. *Wallace*, 306 U. S. 1]. Appellants urge that the Natural Gas Act does not give the Commission jurisdiction over all sales of natural gas in interstate commerce. But the Natural Gas Act does apply, among other things, to 'the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use.' That language exactly covers the sales described in Exhibit F. We cannot disregard the plain language of the statute because the Commission at one time interpreted it narrowly [citing *In the Matter of Columbian Fuel Corporation*, Opinion No. 48, Docket No. G-143, 35 P.U.R. (N.S.) 3], or because the reports of Congressional committees show an intention not to 'disturb' state regulation, or because appellants fear duplicate regulation. The Act applies to 'natural-gas companies engaged in such * * * sale', and defines 'natural-gas company' as a company 'engaged in the transportation of natural gas in interstate commerce, or the sale in interstate commerce of such gas for resale.' * * *

"Appellants have nowhere denied the statements in Paragraph (d) of Exhibit F. Their answer to the Commission's motion denies that the Company is a natural-gas company within the meaning of the Natural Gas Act, and states that it 'does not transport natural

gas in interstate commerce or sell natural gas in interstate commerce for resale for ultimate public consumption for domestic, commercial, industrial, or any other use.' But these denials are in the nature of legal conclusions, since they turn, or may turn, on the meaning of the legal terms 'natural-gas company' and 'interstate commerce.' They cannot be deemed denials of the statements of fact in Exhibit F. * * * During oral argument in the District Court counsel conceded that the Company often sells gas to the New York Company, and impliedly conceded that this gas is sold for transportation to New York and resale. On this appeal counsel again concede that the Company sells to the New York Company gas which it transports to New York. Appellants nowhere suggest that these sales are not 'for resale for ultimate public consumption.' * * *"

After the Peoples Company had filed a petition for rehearing, the Court made this additional comment:

"Appellants urge that the Company's sales to the New York company, for transportation to New York and resale, are not 'sale(s) in interstate commerce' of natural gas for resale within the meaning of the Natural Gas Act. * * * Their position is not that Congress could not, but that it did not, authorize the Commission to regulate such sales. We think the position is untenable.

"The Supreme Court has lately held that sales to distributors of natural gas which has been brought from another state are within the jurisdiction of the Federal Power Commission [citing *Illinois Natural Gas Company v. Central Illinois Public Service Co.*, 314 U. S. 498].

"Sales of gas which has just moved interstate and sales of gas which is about to move interstate have like practical effects. Neither the Committee nor Congress nor the Court appears to have distinguished between them in regard to the application of the Act; in fact the contrary appears. To illustrate the sales which the Act was designed to reach, the Committee referred to two Supreme Court cases. One of these involved sale and delivery after the state line had been crossed; but

the other involved sale and delivery at the state line. [Citing *Public Utilities Commission* v. *Attleboro Steam & Electric Company*, 273 U. S. 83]. And in the recent Illinois Natural Gas case, quoted above, the Court said: '* * * the particular point at which the title and custody of the gas passed to the purchaser without arresting its movement to the intended destination does not affect the essential interstate nature of the business.' Still more recently, in another case upholding the Federal Power Commission's authority under the Act, the Court said: 'The sale of natural gas originating in one state and its transportation and delivery to distributors in any other state constitutes interstate commerce. * * *.' [Citing *Federal Power Commission* v. *Natural Gas Pipeline Company of America*, 315 U. S. 575]. Though that case involved sales in the state of destination, the quoted language governs sales in the state of origin. * * *

"Appellants urge that 'in interstate commerce' is a narrower term than 'in or affecting interstate commerce,' and that Congress did not delegate to the Commission its entire power over natural gas. This is true. Sales which merely 'affect' interstate commerce are outside the Act. But this throws no light on the question whether the Company's sales to the New York Company are 'in' interstate commerce."

The Court of Appeals of the District of Columbia, in its decision in the *Peoples case*, made no reference whatever to the language in Section 1(b) of the Act exempting "the production and gathering of natural gas" from the jurisdiction of the Commission. There was no need for the Court to discuss that question, inasmuch as the Company had in effect admitted that it made a sale for resale of natural gas in interstate commerce[1] and therefore, in the

[1]The sale by the Peoples Company was described by the Company itself as follows: "Gas so sold to New York State Natural Gas Corporation is delivered to that Company at the outlet of the Respondent's Pew Compression Station located in Limestone Township, Clarion County, Pennsylvania, from which point the gas is transported in a northeasterly direction

absence of any detailed explanatory facts of record, there was a sufficient predicate for the Court to hold that the Commission had authority to examine the books and records of the Peoples Company.

It will be noted that the Court of Appeals for the District of Columbia, in the *Peoples case*, cited and relied upon decisions of this Court in gas and electric cases involving the question of what constitute sales in interstate commerce. The *Attleboro* and *Kansas Natural Gas Company cases* have been heretofore discussed in this brief. They were cited in the Congressional committee reports on the Natural Gas Act to illustrate the character of transaction intended to be covered by the Act, namely, the transportation and sale for resale of natural gas in interstate commerce, or so-called wholesale sales. The other cases cited by the Court in the *Peoples case* show clearly that the Court was passing only on the question whether a sale of gas *within* a state, when such gas moves in a continuous stream in interstate commerce, is subject to regulation by the Commission.

In the *Illinois Natural Gas Company case* (314 U.S. 498), this Court had before it the question whether the Illinois Commerce Commission or the Federal Power Commission had jurisdiction to require an extension of facilities by the Illinois Natural Gas Company, whose properties were located wholly within the State of Illinois. The Court held

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a distance of approximately 90 miles to a point in Hebron Township, Potter County, Pennsylvania, through a 12" pipe line owned by the Respondent but leased to and operated by the New York State Natural Gas Corporation under an agreement of lease dated January 2, 1940, at which point said 12" pipe line connects with the pipe lines owned by New York State Natural Gas Corporation. * * * Upon the delivery of the gas by Respondent to New York State Natural Gas Corporation at Respondent's Pew Compressing Station as aforesaid, the gas passes out of the possession of the respondent and thereafter Respondent has no control over the transportation, sale or disposition of said gas." (Answer to Order to Show Cause, Appendix to Appellant's Brief in Court of Appeals for the District of Columbia, p. 36).

that the natural gas purchased by Illinois Natural from its affiliate, Panhandle Eastern Pipeline Company, moved in a continuous stream in interstate commerce, and that therefore the Power Commission had jurisdiction over the extension of facilities involved, under the provisions of the Natural Gas Act. It is clear from this Court's opinion that Illinois Natural owned "transmission" lines, and there was no question involved or discussed in respect to the Federal Power Commission's jurisdiction over production and gathering facilities. As a matter of fact, the discussion of this Court in the *Illinois Natural case* fully corroborates our position that the provisions of the Natural Gas Act were *restricted* to the transportation and sale of natural gas in interstate commerce for resale. This Court said:

> "An avowed purpose of the Natural Gas Act of June 21, 1938, was to afford, through the exercise of the national power over interstate commerce, an agency for regulating the wholesale distribution to public service companies of natural gas moving interstate, which this Court had declared to be interstate commerce not subject to certain types of state regulation. H.R. No. 709, Committee on Interstate and Foreign Commerce, 75th Cong., 1st Sess., April 28, 1937. By its enactment Congress undertook to regulate a defined class of natural gas distribution without the necessity, where Congress has not acted, of drawing the precise line between state and federal power by the litigation of particular cases. *By Section 1(b), 15 U.S.C. Section 717 (b), the Act is restricted* in its *application* to 'the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale. . . .' And by Section 2(6), 15 U.S.C. Section 717a(6) 'natural-gas company' means a person [including a corporation] engaged in the transportation of natural gas in interstate commerce or the sale in interstate commerce of such gas for resale. Sections 4, 5, 6, 15 U.S.C. Section 717, c, d, e, give the Federal Power Commission extensive con-

trol over the rates at which the gas is sold for resale. Under Section 7(a), 15 U.S.C. Section 717f(a) the Commission has authority to order natural-gas companies to extend their systems to establish physical connections of their transportation facilities with those of distributors and to sell gas to them. Section 7(b) prohibits the abandonment of the facilities of natural-gas companies without approval of the Commission. Section 7(c), here involved, provides that 'No natural-gas company shall undertake the construction or extension of any facilities for the tansportation of natural gas to a market in which natural gas is already being served by another natural-gas company, or acquire or operate any such facilities or extensions thereof, or engage in any transportation by means of any new or additional facilities, or sell natural gas in any such market,' without the Federal Commission's certificate of public convenience and necessity.

"We think it plain that these provisions, read in the light of the legislative history, *were intended to bring under federal regulation wholesale distribution, like that of appellant, of gas moving interstate*. Appellant engages in interstate commerce in gas and in its interstate transportation as those terms had been defined by this Court, before the adoption of the Act. After the gas is brought into the state appellant makes the first sale to distributors for resale, to which the Act in terms applies, and which the cases last mentioned defined as a part of the commerce subject in some respects to the exclusive regulation of Congress. *Cf. Parker* v. *Motor Boat Sales, Inc.*, No. 46, decided this term. Section 7 of the Act commits to the Federal Commission the control of extensions and abandonment of the transportation facilities of natural gas companies, their physical connection with those of distributors and sales to distributors, and prohibits extensions, such as the state commission has now ordered, into an area already served by another natural gas company, unless the Commission has first granted a certificate of public convenience and necessity. Since the communities here are supplied by the Universal and Central companies, which transport the gas interstate, they constitute a

market already served by a natural gas company within Section 7(c) and Section 2(6) of the Act.

"The Federal Commission has ruled that it has jurisdiction under the Act over companies which, like appellant, sell at wholesale to local distributors gas moving interstate. *Re Billings Gas Company*, 35 P.U.R. (N.S.) 321; *Re East Ohio Gas Company*, 28 P.U.R. (N.S.) 129. The proceedings of the Commission under Section 7 (c) indicate the many important matters which it takes into consideration in determining whether an extension of facilities in a case such as this should be permitted."

In *Public Utilities Commission of Ohio* v. *United Fuel Gas Company*, 317 U.S. 456, this Court stated that:

"It is clear, as the legislative history of the [Natural Gas] Act amply demonstrates, that Congress meant to create a comprehensive scheme of regulation which would be complementary in its operation to that of the states, without any confusion of functions. The Federal Power Commission would exercise jurisdiction over matters in interstate and foreign commerce, *to the extent defined in the Act*, and local matters would be left to the state regulatory bodies."

The question of the jurisdiction of the Commission over "the production and gathering of natural gas" was not specifically involved in *Federal Power Commission et al.*, v. *Natural Gas Pipeline Company of America et al.*, 315 U.S. 575. In that case, for the purpose of entering an interim order reducing rates, the Commission accepted the companies' evidence in respect to reproduction cost new, the *value* of gas reserves, capital additions and working capital, when it determined a rate base. It also accepted substantially the companies' showing in respect to operating revenues and expenses (except as to the manner of determining annual amortization expense). Accordingly, in that case, there was no occasion for anyone to contest the authority of the Commission over production and gathering

facilities, and the question was not discussed in this Court's opinion. The issue simply was not presented. In connection with its discussion of the constitutionality of the Natural Gas Act, this Court did observe, however, that:

> "The sale of natural gas originating in one state and its *transportation* and *delivery* to distributors in any other state constitutes interstate commerce, which is subject to regulation by Congress."

In *Federal Power Commission et al.* v. *Hope Natural Gas Company*, 320 U.S. 591, the Hope Company raised no question concerning the jurisdiction of the Commission over its production and gathering operations. In respect to leaseholds, the company made its showing on a *cost* rather than a *value* basis and apparently did not desire to press any question concerning the Commission's authority over production and gathering operations. In connection with its discussion of the position of the State of West Virginia, the Court observed (320 U.S. at p. 609: 612):

> "We pointed out in *Illinois Natural Gas Co.* v. *Public Service Co.*, 314 U. S. 498, 506, that the purpose of the Natural Gas Act was to provide, 'through the exercise of the national power over interstate commerce, an agency for regulating the wholesale distribution to public service companies of natural gas moving interstate, which this Court had declared to be interstate commerce not subject to certain types of state regulation.' As stated in the House Report the 'basic purpose' of this legislation was 'to occupy' the field in which such cases as *Missouri* v. *Kansas Gas Co.*, 265 U. S. 298, and *Public Utilities Commission* v. *Attleboro Steam & Electric Co.*, 273 U. S. 83, had held the States might not act. H. Rep. No. 709, 75th Cong., 1st Sess., p. 2. In accomplishing that purpose the bill was designed to take 'no authority from State commissions' and was 'so drawn as to complement and in no manner usurp State regulatory authority.' *Id.*, p. 2. And the Federal Power Commission was given no authority over the 'production or gathering of natural gas.'
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> * * * * *

"We do not mean to suggest that Congress was unmindful of the interests of the producing states in their natural gas supplies when it drafted the Natural Gas Act. As we have said, the Act does not intrude on the domain traditionally reserved for control by state commissions; and the Federal Power Commission was given no authority over 'the production or gathering of natural gas.' Sec. 1(b). In addition, Congress recognized the legitimate interests of the States in the conservation of natural gas. By Sec. 11 Congress instructed the Commission to make reports on compacts between two or more States dealing with the conservation, production and transportation of natural gas."

It is true that the majority opinion of the Court in the *Hope case*, in a footnote (320 U. S. at p. 614), negatived a suggestion (apparently made by the State of West Virginia) that the exemption language in Section 1(b) precluded the Commission from even ascertaining the cost of the production plant, and referred to Section 14(b) of the Act giving the Commission the power to "determine the propriety and reasonableness of the inclusion in operating expenses, capital, or surplus of all delay rentals or other forms of rental or compensation for unoperated lands and leases." However, as pointed out above, the Hope Company had raised no question concerning the Commission's authority over production. In the instant cause, Canadian has from the very outset of the proceeding contested, and still does vigorously contest, the Commission's authority over its production and gathering operations. If the Court's observations in its note to the *Hope case* decision appear to be in conflict with its prior statements, heretofore quoted, definitely stating that the Commission lacks authority over "the production or gathering of natural gas," it seems evident that no such mere dictum in a note should be deemed controlling over specific rulings of the character indicated.

In the instant cause the Commission relies upon certain decisions interpreting its jurisdiction under the Federal

Power Act to support its claim that it rightfully exercised jurisdiction over Canadian's production and gathering operations. We have heretofore pointed out in this brief (footnote on p. 13) that Congress treated the Federal regulation of electric and gas companies as separate and distinct propositions, and legislated separately with respect to the peculiarities of each business. This is apparent, not only from the legislative history of the two Acts, but also from the provisions of the Acts themselves. To illustrate the difference in legislative treatment accorded by Congress to electric and gas operations, we set forth below, in parallel columns, the provisions of Sections 201(a) and (b) of the Federal Power Act (which were involved in the electric cases relied upon by the Commission) and Sections 1(a) and (b) of the Natural Gas Act, which are involved in this proceeding:

Federal Power Act	*Natural Gas Act*
"Section 201. (a) It is hereby declared that the business of transmitting and selling electric energy for ultimate distribution to the public is affected with a public interest, *and the Federal regulation of matters relating to generation to the extent provided in this Part* and the Part next following and of that part of such business which consists of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, such Federal regulation, however, to extend only to those matters which are not	"Section 1. (a) As disclosed in reports of the Federal Trade Commission made pursuant to Senate Resolution 83 (Seventieth Congress, first session) and other reports made pursuant to the authority of Congress, it is hereby declared that the business of transporting and selling natural gas for ultimate distribution to the public is affected with a public interest, and that Federal regulation in matters relating to the transportation of natural gas and the sale thereof in interstate and foreign commerce is necessary in the public interest. "(b) The provisions of this act shall apply to the trans-

subject to regulation by the States.

"(b) The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce, but shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction, *except as specifically provided in this Part and the Part next following, over facilities used for the generation of electric energy* or over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter."

portation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas."

It will be readily observed, from the italicized portion of Sections 201(a) and (b) of the Federal Power Act, that Congress apparently *did not* entirely exclude generation of electric energy from the Commission's jurisdiction under the Federal Power Act. On the contrary, Congress *did* entirely exclude the production and gathering of natural gas from the jurisdiction of the Commission under the

Natural Gas Act, and the Act contains no language whatever even hinting that it was intended to be applicable in any manner to production and gathering operations. This difference in the language of the statutes should be kept definitely in mind in considering the possibility that the electric cases may constitute precedents supporting the Commission's contentions.

Jersey Central Power & Light Company v. *Federal Power Commission*, 319 U.S. 61 involved the question whether the Jersey Central Company was a "public utility" subject to the Commission's jurisdiction under the Federal Power Act. This Court held that the company owned and operated "transmission" facilities which subjected it to the jurisdiction of the Commission, even though the transmission took place wholly within one state, citing and relying upon the decisions of this Court in the *Attleboro* and *Illinois Natural cases, supra*. That acts of "transmission" were involved in the *Jersey Central case* appears beyond question from the language used by this Court, for it said:

> "Further, we think the definition in subsection (e) of 'public utility' covers Jersey Central, since that company owns and operates the *transmission* line to the Raritan and that line, as a result of the interpretation of interstate commerce in the preceding paragraph, is a facility under Commission jurisdiction by the terms of subsection (b)."

Hartford Electric Light Company v. *Federal Power Commission*, 131 F. (2d) 953 (cert. den., 319 U.S. 741) upon which great reliance is placed by the Commission in defending its position in this case, may readily be distinguished from the instant proceeding. The *Hartford case* involved the question whether the company was a "public utility" as defined in the Federal Power Act and as such required to comply with an order of the Commission prescribing a system of accounts. The opinion of the Circuit Court in the *Hartford case*, which held that the company's sales from

generating facilities subjected it to the jurisdiction of the Commission, was predicated in large measure upon the language in Sections 201(a) and (b) of the Federal Power Act vesting the Commission with authority over generation of electric energy and facilities used for such generation, when provided for in the Act. As pointed out, no similar language is contained in the Natural Gas Act, for "the production and gathering of natural gas" was excluded without any qualification whatever. It is true that the Court, in the *Hartford case*, cited and relied upon the decision of the Court of Appeals for the District of Columbia in the *Peoples case*, *supra*, but we believe a proper interpretation of that decision will demonstrate that it did not involve the issue of jurisdiction of the Commission over production and gathering of natural gas under Section 1(b) of the Natural Gas Act.

Since these electric cases did not involve the question of the exercise of rate jurisdiction by the Commission in a field not contemplated by Congress, they can hardly be relied upon to support the contention here made by the Commission.

In the instant proceeding, Canadian does not contest the fact that it is a "natural-gas company," as defined in the Natural Gas Act, for concededly it operates facilities for the transportation and sale of natural gas in interstate commerce. However, even though Canadian is a natural-gas company and, therefore, subject to the Commission's jurisdiction in certain respects, its production and gathering operations have been specifically excluded from the Commission's jurisdiction. This is the gist of its position.

The Circuit Court, in the instant proceeding, in one breath stated that, under Section 1(b) of the Act, the Commission "does not have *express or implied* rate-regulatory jurisdiction of the production and gathering of natural gas," and also that under Section 1(b) Canadian's production and gathering properties and facilities "lie beyond the range of the rate-regulatory jurisdiction of the Commission."

However, in the next breath, the Court concluded that the Commission did not exercise a prohibited jurisdiction over Canadian's production and gathering operations because it did not perform the formal function of prescribing rates and charges covering separately the production and gathering of natural gas. We respectfully submit that this conclusion of the Circuit Court is merely a play upon words, for the Commission could not possibly have exercised a more complete jurisdiction over production and gathering operations than it did in this proceeding. It treated the production and gathering properties of this company in the identical manner in which it treated the company's transportation properties, in respect to rate base, revenues, expenses, return, and all other elements considered—and it frankly said so in its opinion. The Circuit Court, in effect, states that the Commission may lawfully do *indirectly* what it may not do *directly*, without violating the language of the Act. We firmly believe that Congress obviously never intended to erect by such indirect method of avoiding the precise and unequivocal exemption language which it carefully inserted in Section 1(b) of the Act.

The Circuit Court commented further that the "Commission did not attempt to affect in any manner the acquiring and maintaining of gas leaseholds, gas rights, or gas wells." We are convinced that, in making this observation, the Circuit Court confused the meaning of the terms "conservation" and "production" of natural gas. The Commission did not, it is true, attempt to tell Canadian whether it could or should obtain permits from State authorities to drill wells, where or when the wells could be drilled, their spacing in the field, the permissible volume of gas to be taken from the wells, or matters of that nature, which are recognized to be "conservation" measures subject to control by State authorities and definitely affecting the "acquiring and maintaining of gas leaseholds, gas rights, or gas wells." Congress recognized the distinction between "conservation" and "production" of natural gas in the Natural Gas

Act, and excluded *both* from the jurisdiction of the Commission, as was clearly recognized and stated in the majority opinion of this Court in the *Hope case*, *supra* (320 U. S., at p. 613).

The observation of the Circuit Court that the Commission did not "undertake to affect anywise the location, construction and extension, or physical connections of pipelines, or the operation of pipe lines or other facilities constituting the gathering properties" was obviously *obiter dicta*, and must be deemed of no consequence here because there was no such issue involved in this rate-making proceeding. In any event, it is what the Commission did, rather than what it may have refrained from doing, which is at issue in this review.

Although the Circuit Court used language differing from that used by the Commission, it in effect upheld the contention of the Commission—stated with the utmost frankness in its brief before the Circuit Court (page 25)—to the effect that the exception language in Section 1(b) of the Act should be interpreted as follows:

> "The exception, therefore, amounts to saying that whenever necessaty for the purposes specifically provided in subsequent sections of the Act, the Commission shall have jurisdiction over production and gathering, etc.
>
> "Under this construction, the Commission has jurisdiction of production and gathering so far as production and gathering is in aid of sales of natural gas in interstate commerce for resale subject to the rate jurisdiction of the Commission."

At least the position of the Commission is stated with startling candor. In effect, it contends that the exemption language contained in Section 1(b) is *not* an exemption of production and gathering at all. Instead, it would have it that this language means just the opposite, namely, that the Commission *does* have jurisdiction over production and gathering whenever the Commission may be of the opinion

that it should exercise such jurisdiction as an aid to its regulation of sales for resale. Under this interpretation of the Act, the exemption of production and gathering from the Commission's authority becomes meaningless and of no consequence whatever, for all the Commission has to do is to determine that it is "necessary" to assume jurisdiction over production and gathering, and that is all there is to it. A more drastic departure from the express language of the Act, specifically exempting production and gathering from jurisdiction, could not possibly be imagined. Such an interpretation places Congress in the untenable position of saying one thing and really meaning just the opposite.

If the interpretation so urged by the Commission should finally be upheld, what is to prevent this body from regulating also the local distribution of natural gas? The language excluding the production and gathering of natural gas from the Commission's jurisdiction is as broad as is the language in the same subsection (Section 1(b)) excluding the distribution of natural gas from the Commission's authority. Yet the Commission, under the theory so advanced, might conclude it is "necessary" to control local distribution in order to make effective its regulation of sales for resale of natural gas. Following the logic of its contention in this proceeding, the Commission could also exercise jurisdiction over local distribution, and thereby further frustrate the clear legislative intent to the contrary.

Frankly, it is this tendency on the part of this regulatory body to attempt to extend its jurisdiction beyond the scope contemplated by Congress, whenever its philosophy renders it apparently "necessary" so to do, that gives us pause. The Independent Natural Gas Association of America is composed not alone of "natural-gas companies," subject to the Natural Gas Act because of their interstate gas transportation activities, but it has among its members many producers of natural gas who sell such gas at the well-head or at the end of their gathering operations. If jurisdiction over production and gathering—whether it be of a rate-

making character or otherwise—is to be read into this statute, it is our conviction that this should be done by the legislature, rather than by action on the part of the administrators in apparent defiance of the plain language used by Congress in enacting this statute.

This is far from an abstruse issue of mere philosophical import. It reaches into every phase of the business of these gas producers, and would place under federal control each function of that business. If it should be contended that in the instant cause the Commission was entitled to overlook the plain language of Congress because it found it convenient to consider this company's operations overall, in fixing its rates, and if as a result this particular exception should be judicially confirmed, what is to prevent the Commission from taking the next step of holding that a purely production company is a "natural-gas company" under the Act—and fully subject to its jurisdiction—because, forsooth, its gas (sold at the well-head) finds its way eventually into the stream of interstate commerce? Once the first step is taken there will be no end, and "white" will indeed become "black," regardless of the will or intent of Congress. And if this be done (as the Commission's brief hints should be done) discrimination will at once arise as between those producers who sell gas to interstate pipelines and those who do not. This unfortunate result would do great harm to this industry, for he who would preserve the value of his production properties must refrain from making any sales to interstate pipelines. Let us not blind ourselves to these implications of the Federal Power Commission's acts and arguments.

Happily, there is an easy way out of the Commission's apparent difficulty. This is by the adoption in its rate-making proceedings of the allowance in the operating expenses of the natural-gas companies that are unquestionably under its jurisdiction of the "fair field price" or fair market value, as a commodity, of the gas which finds its way into their transmission lines for interstate transportation and

subsequent sale. If the producer and the final transporter are separate companies and act wholly at arm's length, this is precisely what would happen were this Commission to operate as do other rate regulatory bodies. It is as if the gas were coal purchased by an electric generating company, or pencils bought for its office, or—indeed—labor which it employs in its operations.

So long as the transaction is fair, and the price paid for the gas, or coal, or pencils, or labor is a fair price, every aim of proper rate-making is appropriately fulfilled by such action. And the allowance of a fair amount for such gas, as a commodity, offers the simple, and, we believe, the sound solution of its problem to this agency.

In the ordinary case of a sale at arm's length by separate entities, the price fixed for the gas in question may reasonably be presumed to be its fair market value, as a commodity, in the field. Should there be any doubt or suspicion on this point, the Commission is clearly not left helpless, for it may of course examine into the situation, and if the price be found to be exorbitant, under all the circumstances, it may provide for the allowance, *in the transportation company's operating expense*, of only that sum which would be the fair market price. This is as true of gas so purchased as it is of coal or any other commodity used in the regulated business.

And where "affiliation" is involved, the sole difference is that the burden might be shifted to the contracting parties to prove that the price in question is a fair price for the gas, as a commodity, in the gas field under consideration and at the time the sale in question is being made. Here again, recognized principles of administrative operation apply, and the rights and interests of the Commission as well as of the public and of the regulated company and its vendor are fully preserved by the power to fix the reasonable operating expense to be allowed for such purchases of gas in fixing the rates of the vendee, the interstate transporter.

The instant cause is but one step removed from such a situation. Here both the producing and the transporting

facilities are owned by the same entity. Yet here, also, the reasonable price of gas, as a commodity, in the field in question, and at the time the gas is put into the transmission lines, represents the fair allowance of operating expense for this commodity. We shall discuss this subject more fully in the next subdivision of this brief, but at this point we believe the above series of illustrations is of import, since it discloses how readily the Commission's apparent difficulty can be solved without in anywise doing violence to the statute, or to the will of Congress as expressed in the exemption of production and gathering from Federal Power Commission jurisdiction.

Were any other principle to be adopted, we would inevitably witness the fixing and allowance of a multiplicity of different prices for the gas of different companies (some only producers, some "affiliated" with transporters, and some both producers and transporters), though the gas be produced in the same field and at the same time. Any course which involves a procedure other than the allowance of the "fair field price," as an operating expense of the transporter, will inevitably serve only to penalize the more efficient or those who, by early entrance into the field or otherwise, have been able to obtain leases on a less costly basis than the later comers. The considerations outlined in the next subdivision of this brief, will—we believe—disclose that such a course in respect to this particular business, is emphatically not in the public interest.

III. Assumption of Jurisdiction by the Commission over Production and Gathering Has a Direct Effect Upon the Value of Natural Gas in the Field.

The Commission seems firmly and apparently irrevocably committed to a practice and policy, in rate cases arising under the Natural Gas Act, of a determination of "cost" rather than "value," even in respect to production property such as gas leaseholds. In the case under review, the

Commission gave no consideration whatever to Canadian's uncontradicted evidence that the market value of its leaseholds (excluding wells) amounted to over $15,000,000 (Ex. 181; R., V. 6, 3181-3254). Instead, the Commission found the depreciated cost of the leaseholds to be a sum less than $1,000,000, based upon the testimony of its own staff witness (Ex. 146, p. 62-64; R. V. 5, 2717-2721; R., V. 1, 186). This was the only amount included in Canadian's rate base for gas leaseholds.

The Commission also failed to give any weight whatever to testimony concerning the fair market value of gas, as a commodity, at the well-head in the Panhandle (Texas) Gas Field, although the record contains ample evidence to the effect that such market value ranges from 3.6 cents to 4 cents per thousand cubic feet. There is also evidence in the record to the effect that the market value of Canadian's gas at the end of its gathering line is approximately 7 cents per thousand cubic feet (R., V. 6, 3255-3281).

The inevitable consequence of following the Commission's cost theory in respect to production property is to lower the field prices of natural gas to an extent which may prevent or greatly curtail exploratory operations for the discovery of new sources of gas supply.[1] As was so forcefully

[1] In the 1943 Report of the Committee on Natural Gas, Section of Mineral Law, American Bar Association, it was stated that: "The Mineral Law Section is interested primarily in problems of production. Regulation of a public utility character concerns the Public Utility Section. However, the effect on production of the Natural Gas Act deserves study. Especially worthy of attention is the attitude of the Commission toward its jurisdiction over production and gathering. The mere contemplation of Federal Power Commission regulation of the well-mouth price of gas which finds its way into interstate commerce makes thousands of individual producers shudder. The principles of cost, adopted by the Commission in its rate-fixing activities would eliminate forever discovery value, would limit the financial recovery to cost plus 6½ per cent and take away all incentives to wildcat operations. Losses incurred in unsuccessful projects could not be balanced out against the cost of other and different successful projects.

and cogently pointed out by Mr. Justice Jackson in his separate opinion (concurred in by Mr. Justice Frankfurter) in the *Hope case, supra,* the natural gas business is wholly unlike ordinary public utility services such as are involved in railroad, bus, steamship, communication, electric or manufactured gas operations. Natural gas is an exhaustible resource, the supply of which can only be replenished by a continuous process of new discoveries, and Mr. Justice Jackson aptly observed in the *Hope case* "the wealth of Midas and the wit of man cannot produce or reproduce a natural gas field" (320 U.S., at p. 629). In that case, the Company did not make any claim for the "value" of its leaseholds, but relied instead only upon their cost (320 U.S., at p. 645), and did not dispute the action of the Commission in including its production and gathering operations within the scope of the rate proceeding. On the other hand, in the instant case, Canadian has throughout the proceedings, before the Commission and the Circuit Court, earnestly contended that the Commission erred when it considered Canadian's production and gathering operations and dealt with them as it did. In addition, Canadian offered uncontradicted evidence in respect to the value of its leaseholds and the fair market value of the gas in the field. Mr. Justice Jackson's comments in the *Hope case* in respect to a correct approach to the determination of field prices for natural gas, appear particularly pertinent to the instant case, and we deem it fitting to quote from them at some length. Among other things, he said (320 U.S., at p. 647 et seq.):

> "Hope's business has two components of quite divergent character. One, while not a conventional common-carrier undertaking, is essentially a transportation enterprise consisting of conveying gas from where it is

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Two wells each costing the same but one producing twice as much as the other would result in the price of gas from one well being twice that of the other. It is not too much to say that the economic incentive for the small producer engaged in widely separated projects would be gone."

produced to a point of delivery to the buyer. This is a relatively routine operation not differing substantially from many other utility operations. The service is produced by an investment in compression and transmission facilities. Its risks are those of investing in a tested means of conveying a discovered supply of gas to a known market. A rate base calculated on the prudent investment formula would seem a reasonably satisfactory measure for fixing a return from that branch of the business whose service is roughly proportionate to the capital invested. But it has other consequences which must not be overlooked. It gives marketability and hence 'value' to gas owned by the company and gives the pipeline company a large power over the marketability and hence 'value' of the production of others.

"The other part of the business—to reduce to possession an adequate supply of natural gas—is of opposite character, being more erratic and irregular and unpredictable in relation to investment than any phase of any other utility business. A thousand feet of gas captured and severed from real estate for delivery to consumers is recognized under our law as property of much the same nature as a ton of coal, a barrel of oil, or a yard of sand. The value to be allowed for it is the real battleground between the investor and consumer. It is from this part of the business that the chief difference between the parties as to a proper rate base arises.

"Is it necessary to a 'reasonable' price for gas that it be anchored to a rate base of any kind? Why did courts in the first place begin valuing 'rate bases' in order to 'value' something else? The method came into vogue in fixing rates for transportation service which the public obtained from common carriers. The public received none of the carriers' physical property but did make some use of it. The carriage was often a monopoly so there were no open market criteria as to reasonableness. The 'value' or 'cost' of what was put to use in the service by the carrier was not a remote or irrelevant consideration in making such rates. Moreover the difficulty of appraising an intangible service was thought to be simplified if it could be related to physical property which was visible and measurable

and the items of which might have market value. The court hoped to reason from the known to the unknown. But gas fields turn this method topsy turvy. Gas itself is tangible, possessible, and does have a market and a price in the field. The value of the rate base is more elusive than that of gas. It consists of intangibles—leaseholds and freeholds—operated and unoperated—of little use in themselves except as rights to reach and capture gas. Their value lies almost wholly in predictions of discovery, and of price of gas when captured, and bears little relation to cost of tools and supplies and labor to develop it. Gas is what Hope sells and it can be directly priced more reasonably and easily and accurately than the components of a rate base can be valued. Hence the reason for resort to a roundabout way of rate base price fixing does not exist in the case of gas in the field.

"But if found, and by whatever method found, a rate base is little help in determining reasonableness of the price of gas. Appraisal of present value of these intangible rights to pursue fugitive gas depends on the value assigned to the gas when captured. The 'present fair value' rate base, generally in ill repute, is not even urged by the gas company for valuing its fields.

"The prudent investment theory has relative merits in fixing rates for a utility which creates its service merely by its investment. The amount and quality of service rendered by the usual utility will, at least roughly, be measured by the amount of capital it puts into the enterprise. But it has no rational application where there is no such relationship between investment and capacity to serve. There is no such relationship between investment and amount of gas produced. Let us assume that Doe and Roe each produces in West Virginia for delivery to Cleveland the same quantity of natural gas per day. Doe, however, through luck or foresight or whatever it takes, gets his gas from investing $50,000 in leases and drilling; Roe drilled poorer territory, got smaller wells, and has invested $250,000. Does anybody imagine that Roe can get or ought to get for his gas five times as much as Doe because he has spent five times as much? The service one renders to

society in the gas business is measured by what he gets out of the ground, not by what he puts into it, and there is little more relation between the investment and the results than in a game of poker.

"Two-thirds of the gas Hope handles it buys from about 340 independent producers. It is obvious that the principle of rate-making applied to Hope's own gas cannot be applied, and has not been applied, to the bulk of the gas Hope delivers. It is not probable that the investment of any two of these producers will bear the same ratio to their investments. The gas, however, all goes to the same use, has the same utilization value and the same ultimate price.

"To regulate such an enterprise by undiscriminatingly transplanting any body of rate doctrine conceived and adapted to the ordinary utility business can serve the 'public interest' as the Natural Gas Act requires, if at all, only by accident. Mr. Justice Brandeis, the pioneer juristic advocate of the prudent investment theory for man-made utilities, never, so far as I am able to discover, proposed its application to a natural gas case. On the other hand, dissenting in *Pennsylvania* v. *West Virginia*, he reviewed the problems of gas supply and said, 'In no other field of public service regulation is the controlling body confronted with factors so baffling as in the natural gas industry; and in none is continuous supervision and control required in so high a degree.' 262 U.S. 553, 621. If natural gas rates are intelligently to be regulated we must fit our legal principles to the economy of the industry and not try to fit the industry to our books.

"As our decisions stand the Commission was justified in believing that it was required to proceed by the rate base method even as to gas in the field. For this reason the Court may not merely wash its hands of the method and rationale of rate making. The fact is that this Court, with no discussion of its fitness, simply transferred the rate base method to the natural gas industry. It happened in *Newark Natural Gas & Fuel Co.* v. *City of Newark, Ohio*, 242 U.S. 405 (1917), in which the company wanted 25 cents per m.c.f., and

under the Fourteenth Amendment challenged the reduction to 18 cents by ordinance. This Court sustained the reduction because the court below 'gave careful consideration to the questions of the value of the property at the time of the inquiry,' and whether the rate 'would be sufficient to provide a fair return on the value of the property.' The Court said this method was 'based upon principles thoroughly established by repeated decisions of this court,' citing many cases, not one of which involved natural gas or a comparable wasting natural resource. Then came issues as to state power to regulate as affected by the commerce clause. *Public Utilities Commission* v. *Landon*, 249 U.S. 236 (1919); *Pennsylvania Gas Co.* v. *Public Service Commission*, 252 U.S. 23 (1920). These questions settled, the Court again was called upon in natural gas cases to consider state rate-making claimed to be invalid under the Fourteenth Amendment. *United Fuel Gas Co.* v. *Railroad Commission of Kentucky*, 278 U.S. 300 (1929); *United Fuel Gas Company* v. *Public Service Commission of West Virginia*, 278 U.S. 322 (1929). Then, as now, the differences were 'due chiefly to the difference in value ascribed by each to the gas rights and leaseholds.' 278 U.S. 300, 311. No one seems to have questioned that the rate base method must be pursued and the controversy was as to what rate base must be used. Later the 'value' of gas in the field was questioned in determining the amount a regulated company should be allowed to pay an affiliate therefor—a state determination also reviewed under the Fourteenth Amendment. *Dayton Power & Light Company* v. *Public Utilities Commission of Ohio*, 292 U.S. 290 (1934); *Columbus Gas & Fuel Co.* v. *Public Utilities Commission of Ohio*, 292 U. S. 398 (1934). In both cases, one of which sustained, and one of which struck down a fixed rate the Court assumed the rate base method, as the legal way of testing reasonableness of natural gas prices fixed by public authority, without examining its real relevancy to the inquiry.

"Under the weight of such precedents we cannot expect the Commission to initiate economically intelligent methods of fixing gas prices. But the Court now

faces a new plan of federal regulation based on the power to fix the price at which gas shall be allowed to move in interstate commerce. I should now consider whether these rules devised under the Fourteenth Amendment are the exclusive tests of a just and reasonable rate under the federal statute, inviting reargument directed to that point if necessary. As I see it now I would be prepared to hold that these rules do not apply to a natural gas case arising under the Natural Gas Act.

"Such a holding would leave the Commission to fix the price of gas in the field as one would fix maximum prices of oil or milk or coal, or any other commodity. Such a price is not calculated to produce a fair return on the synthetic value of a rate base of any individual producer, and would not undertake to assure a fair return to any producer. The emphasis would shift from the producer to the product, which would be regulated with an eye to average or typical producing conditions in the field.

"Such a price fixing process on economic lines would offer little temptation to the judiciary to become back seat drivers of the price fixing machine. The unfortunate effect of judicial intervention in this field is to divert the attention of those engaged in the process from what is economically unwise and self-defeating limits before they would reach constitutional ones. Any constitutional problems growing out of price fixing are quite different than those that have heretofore been considered to inhere in rate making. A producer would have difficulty showing the invalidity of such a fixed price so long as he voluntarily continued to sell his product in interstate commerce. Should he withdraw and other authority be invoked to compel him to part with his property, a different problem would be presented.

"Allowance in a rate to compensate for gas removed from gas lands, whether fixed as of point of production or as of point of delivery, probably best can be measured by a functional test applied to the whole industry. For good or ill we depend upon private enterprise to

exploit these natural resources for public consumption. The function which an allowance for gas in the field should perform for society in such circumstances is to be enough and no more than enough to induce private enterprise completely and efficiently to utilize gas resources, to acquire for public service any available gas or gas rights and to deliver gas at a rate and for uses which will be in the future as well as in the present public interest."

Several of the large natural gas producing states are today attempting to obtain an increased value for the natural gas resources in their respective states. This Court is intimately familiar with the contentions raised by the State of West Virginia in the recent *Hope case*. It appears that the Railroad Commission of Texas, the gas regulatory body in the largest gas-producing state in the nation, also advocates a larger market and a higher price for its natural gas, for counsel for that Commission, in a certificate proceeding before the Federal Power Commission (*In the Matter of Memphis Natural Gas Company*, Opinion No. 119, quoted at p. 21) recently stated that:

> "We are great marketers of natural gas in Texas and we feel that the better the market, the larger the market, the better the price, and the better the price, the easier it is to prevent physical waste of natural gas, because then you have landowners and everyone else undertaking to prevent waste and hold it down."

It is certainly logical to contend that Congress, when it exempted production and gathering from the provisions of the Act, intended to leave the price of natural gas in the field to be determined by economic and competitive factors rather than by regulation on an individual "cost" basis by the Commission. It is well known that the acquisition of leaseholds and the sale therefrom of natural gas is generally a highly competitive business. Such competition will ordinarily establish a "going" price for natural gas in the

field, as a commodity, and to that extent extraneous regulation would be rendered unnecessary. Congress, when it enacted the Natural Gas Act, had before it a full report from the Federal Trade Commission on the natural gas industry, which was referred to in Section 1(a) of the Act. In this report, the Federal Trade Commission commented that the "field price is based upon competition rather than a real cost-plus basis," and it was cogently added that there is "no positive relationship between costs of drilling wells and the selling price of gas." (Sen. Doc. No. 92 Part 84-A, p. 132, 70th Cong., 1st Sess.)

Indeed, Mr. Dozier Devane, then Solicitor of the Federal Power Commission, stated at the Congressional hearings on the legislation here in question that in this Act "there is no control of the gathering rate; the Commission would not have jurisdiction. *That price is fixed by competitive conditions that exist in the field.*" (Hearings on H.R. 11662, House Committee on Interstate and Foreign Commerce, 74th Cong., 2nd Sess., pp. 42-43).

Under the rulings which the Commission has consistently made in natural gas rate proceedings, however, "cost" testimony alone is considered to be relevant in the determination of field prices of natural gas. Such a cost theory, we submit, is entirely unsuited to the natural gas production business, as was pointed out by Mr. Justice Jackson in his separate opinion in the *Hope case*. Unless this Court should now correct the action of the Commission in this proceeding, the same erroneous "cost" theory will unquestionably continue to be applied by the Commission, to the serious detriment of producers of natural gas, to the detriment of the interests of natural gas producing states, and of the proper conservation of natural gas.

In view of the specific language used by the Congress in Section 1(b) of the Natural Gas Act, as recognized both in the majority and minority opinions of this Court in the *Hope case* where it was said that "the Federal Power Commission was given no authority over 'the production or

gathering of natural gas'" (320 U. S. at pp. 610 and 612), it would seem appropriate, and indeed necessary, for this Court to rule (now that the issue is for the first time squarely before it) that Congress meant precisely what it said in respect to production and gathering, and that the Commission has exceeded its statutory authority in this proceeding. Such a ruling would restore the Natural Gas Act, and the Commission's jurisdiction thereunder, to the proper sphere contemplated by Congress.

IV. The Curious Argument that the Commission's Action Really Does Not Constitute Regulation of Production or Gathering.

The Federal Power Commission was at least forthright. It said that it was "indispensable" for it to cover all of this company's production and gathering properties into the rate base, and all of its production and gathering operations into the operating expense allowances. And, of course, the production and gathering elements figured therefore in the allowed revenues or "return." The Commission did all this frankly and openly, with neither compunction nor dissimulation. It simply included production and gathering, along with transportation, and declared that it did this because these operations were "integrated," and because it saw no way out other than to proceed as it did, apparently regardless of the statute. Such action, it declared, was "indispensable."

The Circuit Court of Appeals, on the other hand, admitted that the Commission is without power to regulate either the operations of production and gathering or the rates therefor. But, said the Court, the Commission didn't really do that, because it didn't fix separate rates for production or for gathering, or for the gas at the conclusion of those operations and at the inception of transportation, but rather merely lumped everything together and fixed rates only for gas at the conclusion of the transportation. Therefore, said

the Court, the Commission did not exercise a jurisdiction or power prohibited by the statute.

We are confronted therefore with a case where (1) the company says "You have exercised a prohibited power. You have taken jurisdiction over our production and gathering operations, and in truth and effect you have fixed rates therefor. This is contrary to the law"; (2) the Commission says, "We had to do it—just couldn't see how we could get around it," and (3) the Circuit Court says, "The Commission can't regulate production and gathering, and it can't make rates for production and gathering. But in this case it didn't really do that,—it merely added up all the company's operations, including those of production and gathering, and fixed a rate for gas at the end of the pipeline. That wasn't prohibited."

Frankly, this situation seems to us much like the old Mexican shell game—now you see the pea, and now you don't. The Commission cannot regulate production and gathering or make rates for gas merely produced and gathered; but it may accomplish the same end, in effect and in truth and fact, by considering the production and gathering as a part of the transportation, over which it does have rate-making power, and by merely fixing the rate for the gas at the conclusion of the entire train of operations.

Let us analyze this curious situation, first under ordinary and usual regulatory and administrative principles, and then in the light of the particular nature of the natural gas business. We believe that in both instances a similar conclusion must be reached. In any event, it should not prove difficult,—certainly not impossible,—to locate the pea under the right shell, and at least we may be pardoned for trying.

First, what is it that a regulatory body does when it fixes the rates to be charged by a regulated entity? If it appropriately follows this Court's injunctions, it seeks first to determine the fair allowance by way of "return" which the company should be permitted to earn as a result of the

services rendered or the commodities sold, and then it endeavors to establish a reasonable "spread" of rates (for the different services offered to different classes of patrons) which will—overall—produce such appropriate return. The vital element is the establishment of allowable "return." If a company is engaged in two businesses, one subject to regulation and the other not, or if it is engaged in both intrastate and interstate business, only one of which is subject to regulation by the Commission in question, the regulatory body may not lump everything together and because of some supposed difficulty of segregation fix the rates for all willy-nilly. On the contrary, it must "separate" the one from the other, and then proceed to determine the proper rates for the service over which it has jurisdiction, as if that were an entirely separate and distinct business. It considers the rate base in that phase of the business, its proper operating expenses and the "return" which would be fair. If the company is losing money in the other (unregulated) phase of its business, it cannot expect to make up those losses by loading them onto the patrons of its regulated services. Nor, if it is making large returns from that other business, can the patrons of its regulated operations expect to obtain their services at otherwise unduly low rates, or possibly free. The two phases of operation must be treated separately.

These principles are universally recognized. In the complex field of telephone service, this Court brought them into play in the *Lindheimer case*,[1] in which a fair "separation" of intra from interstate property, expense and revenue was required before judging the fairness of certain intrastate rates fixed by a state commission. And in such instances as the ownership by a regulated corporation of both a hotel and a motor bus line, and an infinitude of others, the identical principle is necessarily applied. Before the primary

[1] See *Lindheimer* v. *Illinois Bell Telephone Co.*, 292 U. S. 151, and related decisions. *Smith* v. *Illinois Bell Telephone Co.*, 282 U. S. 133, and *Illinois Bell Telephone Co.* v. *Gilbert*, 3 F. (Supp.) 595.

function of determining the proper allowable "fair return" for the regulated portion of such a business can be performed, the regulatory body must fairly and reasonably separate out the properties and the expenses of the phase of the overall corporate operations over which it has jurisdiction. In no other manner can it lawfully or properly exercise its regulatory functions.

Nor could it with logic or propriety say, "We know we have no regulatory power over the charges to be made for the hotel services of this company when we fix its motor bus rates, but we just can't somehow seem to segregate the two, so we will deem it 'indispensable' to lump them together and then we will fix an overall fair return. Of course, we'll actually establish by order only the motor bus rates, but since the hotel is paying nicely we can fix the rates to bus patrons very low and still the company will earn enough overall to keep its head above water." No one would be found to support such a plan or program.

But it may be argued that natural gas is a commodity that is sold, rather than a service that is rendered, and that this fact somehow takes the case out of the general principle. Let us test this proposition. Suppose a natural gas field with ten wells, each capable of producing a million cubic feet of gas per day. The ten separate owners of these wells have each sought a market for their gas, and by the balancing operation of supply and demand a well-recognized "field price" has come into play in this field. All other things being equal, no such owner could hope to sell his gas for more—at least not much more—than this established field price. And certainly he would not sell it for a lower price, unless for some reason of lack of quality or pressure or because of his well's location he could not find a purchaser at the going rate. A pipeline company seeking a source of supply would be perfectly justified in contracting to buy gas in that field at that rate, and in the regulation of its charges to its patrons (after transportation to a distant

market) the properly allowable expense for gas so purchased would be that going rate.

And this would be true irrespective of the individual costs to the well owners of their leases and well properties, though these costs might—and doubtless would—have varied considerably, depending on when they entered the field and whether drilling costs were up or down when they sank their particular wells. A "cost plus" allowance system, if adopted by some short-sighted regulatory body, would result only in confusion, a multiplicity of different rates in the same gas field, and—in the end—in much harm to the public interest, even if if possessed jurisdiction so to do.

The situation is the same if one of the producers and gatherers is the pipeline company itself. To require that its own gas go into the pipeline on a "cost plus" basis, while gas from other producers enters the line on a market price basis could not fail, in the end, to produce confusion and harm to the public interest. Yet this is exactly what the Commission did in the instant case. And the fact that gas is a commodity, rather than a service, not only does not alter the need for a fair "separation" of functions in the fixing of rates, but particularly emphasizes the essentiality of such action, and for the taking into the transmission line of produced and gathered gas (regardless of who did the producing and gathering) at the fair commodity price of such gas in the field, plus a fair amount for the gathering of the gas.

The Commission would of course have to make this segregation if this company sold a portion of its produced and gathered gas in the state of its production, and the remainder went into the channels of interstate commerce. (As, indeed, we understand is the fact with respect to Canadian.) And we apprehend that no one would suggest this this Federal Commission could avoid such segregation upon some imagined "indispensability" of lumping all of the company's operations together when fixing the rates for its interstate business. The case is similar with respect to these operations of production and gathering, which Con-

gress has excepted from this Commission's powers as fully as the company's intrastate sales and operations are excepted by virtue of the Federal Constitution. It is no more difficult to make the one segregation than it is the other,—in fact, the segregation of production and gathering is much more simple, since the effective "short cut" of using the fair field price of the gas, as a commodity, at the inception of transportation is here available to the regulatory body. When a proper "separation" has been made, the regulated phase of the business is readily considered and dealt with by the regulatory body, whether the operation be that of a service or that of a sale of a commodity, while the laws of supply and demand are left to play their part with the remainder, just as if it were in fact operated by a distinct entity.

The case now before the Court presents just such a situation. Here Congress has vested certain rate regulatory jurisdiction in the Federal Power Commission, but in the same breath it has declared that such power shall not go to the operations of production and gathering. If this were a case of two distinct types of service, one subject to regulation and the other not, the necessity for a reasonable segregation of properties, expense and revenue in respect to the two in the fixation of rates for the regulated service would be obvious. It seems no less obvious where the two functions deal with a commodity. If the functions of transportation, on the one hand, were performed by an entity entirely separate and distinct from that which performs those of production and gathering, the going market price of gas at the inception of transportation would obviously be the proper allowance for the gas there purchased, as an operating expense. *And a different allowance where the several functions are operated by a single entity cannot possibly be other than a direct "regulation" of the functions over which jurisdiction has not been granted.*

Here, then, is the shell under which lies the pea. It is idle to say that, merely because specific, separate rates have not been fixed—as such—for production or gathering, the Commission has not effectively exercised rate-making

functions over those operations. For, in effect, the Commission by its action in this case has fixed rates at the inception of transportation as fully and as completely as if it had set them out in black and white. By not adopting the fair market price of the gas, as a commodity, at that point, it has accomplished precisely that exact effect.

Indeed, the fallacy of the Circuit Court's position seems readily demonstrable. It declared that the Commission could not fix this company's rates in respect to its production and gathering operations, but it reasoned that, since the Commission's final rate order set forth only rates to be charged at the conclusion of transportation, the production and gathering rates were not fixed, though the production and gathering properties and expenses were lumped into the figures used in developing the rates which were fixed. The test must be whether this operation established, as one of its necessary effects, the values and amounts at which the produced and gathered gas goes into the transportation system. If that gas had been separately owned and had been purchased by the transporting company at the inception of transportation, the rate base would have included only the transportation properties, and the allowable expenses would have been those of the transportation only, plus the price paid for the gas where it entered the transportation pipeline. And if, in the present case, the Commission had dealt only with the company's transportation properties in establishing the rate base, and had developed only the company's transportation costs in finding operating expenses, it would then have had to adopt—and "fix"—an amount to be allowed for the produced and gathered gas at the inception of transportation. Had this been stated by it separately, no one would doubt but that it had, in effect, "fixed rates for production and gathering."

The Commission's adopted method had this precise necessary effect. It did not state this amount separately, but it lumped everything into one pot and applied a single formula to all,—i. e., it allowed a return of 6½% on the entire rate base, plus overall operating expenses. If we now

subtract from the rate base the amounts covering transportation properties and the expenses attributable to transportation, we find that—under the formula—a certain return was allowed for such operation. The remainder is the rate base fixed for production and gathering properties, and the expenses incident to production and gathering, and—under the formula—the return allowed on such operations.

The making of rates is primarily a process of the ascertainment of reasonably allowable earnings,—the so-called "fair return" of a regulated enterprise. Once this figure is ascertained, the actual individual rates to be charged are largely developed by mere mathematical processes. Here the Commission unquestionably developed, used and promulgated a "return" applicable to the production and gathering operations. To say that production and gathering rates were not "fixed," because the schedule of rates actually set up was for charges after transportation had been performed, including production and gathering, is to blind one's eyes to solid fact. Those rates were in part rates for production and gathering as fully and completely as if they had been stated in two parts. We earnestly submit that the Circuit Court merely begged the question, and erred in fact and in law when it said that the Commission did not in this case fix rates for production and gathering.

The real question is how much shall properly be allowed, over and above the expenses of transportation, for the gas taken into the transmission pipeline. Any lumping of everything together necessarily "fixes a rate" for such gas. And if the exemption of production and gathering from the Commission's jurisdiction means anything, it must mean that such overall action is prohibited. Should fraud, undue influence, unfairly high prices or other similar factors be found to be present, where the producer and the transporter are separate entities, the Commission may deal with the situation through its power to allow, as an operating expense, only the fair market value of purchased gas,

as a commodity. And in cases where the producer and the transporter are the same entity, this same simple principle should be applied.

The Circuit Court therefore erred in its pronouncement in this case to the effect that, though the fixing of production and gathering rates was not a prerogative of the Federal Power Commission, that body had not by its action in respect to this company contravened the statute by exercising a prohibited jurisdiction.

CONCLUSION.

Finally, the Independent Natural Gas Association of America suggests that the problem which is considered in this brief is essentially a relatively simple issue. If, as we believe, jurisdiction over production and gathering has been wholly withheld from the Federal Power Commission, and if, as we further believe, such lack of jurisdiction is all-embracing, the Commission is not faced with an insoluble problem, nor is it "indispensable" for it to commit intellectual mayhem on the statute, as it seemingly did in the instant proceeding. In a case of "integrated" operations, such as this, the allowance as an operating expense of a fair field price for gas at the point of its entrance into the transmission system (i. e., after the conclusion of production and gathering), and the omission of production and gathering properties from the "rate base" and of production and gathering expense from operating expenses, would protect every legitimate interest of the company, the Commission and the public. In the case of separately owned and operated production and gathering properties, this is precisely what would occur, and in the light of the limitation on jurisdiction contained in the Act, this seems to represent a sound, overall policy for universal application.

Moreover, even were it to be held that the Commission's contention is correct to the effect that sales from the wellhead or from a gathering system, when the gas so sold is eventually transported by the vendee to and sold by it in

another state, are "sales in interstate commerce," and are therefore committed to the Commission for regulation, no alteration of the principle just mentioned would apparently be either necessary or justified. As Mr. Justice Jackson has so cogently explained, in his separate opinion in the *Hope case*, natural gas is a unique commodity, and the use of a fair field price at the commencement of transportation represents the soundest method of handling this difficult regulatory problem. Under such a program, production and gathering properties and expenses would simply not be considered, but the going rate for gas in the field would be allowed as an operating expense. On the other hand, if it should be felt that the production and gathering properties should, for any reason, be included in the rate base, then they should be included at their current field values. Only thus may the economic issues which surround the resolution of this problem be fairly and reasonably subserved. This is no mere "Smyth v. Ames" issue. It is far more fundamental than that. It relates not only to the statutory limits of this regulatory body's powers, but also to the basic economy of the entire natural gas industry.

Appropriate judicial determination of this issue of production and gathering jurisdiction, and of the scope of the Federal Power Commission's authority in respect to such operations, is particularly essential at this time. The Commission, in recent pronouncements, and in its brief before the Circuit Court in this proceeding, has apparently taken the position that, despite the express exemption of production and gathering from the purview of the Natural Gas Act, it should assume at least certain powers over such operations in all instances in which gas sold by producers or gatherers is eventually transported in interstate commerce by the vendee. Yet on December 30, 1944, the Commission wrote to Governor Andrew F. Schoeppel (of Kansas), Chairman of the Interstate Oil Compact Commission, that it "has no desire to extend its jurisdiction to cover the production of natural gas or *otherwise* invade

what are properly regarded as the functions of the conservation authorities of the several states," and that "the Commission has no desire to interfere with the several states in the full and effective exercise of their authority regarding either the production or local distribution of natural gas." (Release No. 2607 (G-700) for publication on January 3, 1945.)

Reconcilement of these apparently conflicting expressions seems impossible on any reasonable basis, since the regulation of production and gathering which was undertaken in the instant proceeding (through the allowance of "cost" only, rather than the fair field price, or value of the produced gas, as a commodity) could hardly fail to impinge on the local situation through its effect on field prices and thus upon conservation practices. The members of the Independent Natural Gas Association of America therefore believe it essential that the issue be soundly resolved at this time, and because the intent and will of Congress seems so clearly expressed in this statute, it is respectfully submitted that the judgment of the Circuit Court of Appeals in this cause should be reversed, on the ground that that Court erroneously determined that the Federal Power Commission did not exercise prohibited jurisdiction over Canadian's production and gathering operations, and on the further ground that, even if such exercise of jurisdiction was not in fact prohibited, its exercise was improper, unlawful, and in contravention of this company's rights under the Federal Constitution.

Respectfully submitted,

Independent Natural Gas Association of America,
amicus curiae,

CARL I. WHEAT,
ROBERT E. MAY,
520 Shoreham Building,
Washington 5, D. C.,
Attorneys for said
amicus curiae

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APPENDIX.

The pertinent provisions of the Natural Gas Act of 1938, c. 556, 52 Stat, 821 (15 U.S.C. 717 et seq.), are as follows:

SECTION 1. (a) As disclosed in reports of the Federal Trade Commission made pursuant to Senate Resolution 83 (Seventieth Congress, first session) and other reports made pursuant to the authority of Congress, it is hereby declared that the business of transporting and selling natural gas for ultimate distribution to the public is affected with a public interest, and that Federal regulation in matters relating to the transportation of natural gas and the sale thereof in interstate and foreign commerce is necessary in the public interest.

(b) The provisions of this act shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural-gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.

SECTION 2. (6) "Natural-gas company" means a person engaged in the transportation of natural gas in interstate commerce, or the sale in interstate commerce of such gas for resale.

(7) "Interstate commerce" means commerce between any point in a State and any point outside thereof, or between points within the same State but through any place outside thereof, but only insofar as such commerce takes place within the United States.

SECTION 4. (a) All rates and charges made, demanded, or received by any natural-gas company for or in connection with the trans-

portation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) No natural-gas company shall, with respect to any transportation or sale of natural gas subject to the jurisdiction of the Commission (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from the date this act takes effect) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulation, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect.

The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, or State commission, or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect: *Provided*, That the Commission shall not have authority to suspend the rate, charge, classification, or service for the sale of natural gas for resale for industrial use only; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period, on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective, the Commission may, by order, require the natu-

ral-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible.

SECTION 5. (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however*, That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural gas company; but the Commission may

order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

(b) The Commission upon its own motion, or upon the request of any State commission, whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transportation of natural gas by a natural-gas company in cases where the Commission has no authority to establish a rate governing the transportation or sale of such natural gas.

SECTION 7. (a) Whenever the Commission, after notice and opportunity for hearing, finds such action necessary or desirable in the public interest, it may by order direct a natural-gas company to extend or improve its transportation facilities, to establish physical connection of its transportation facilities with the facilities of, and sell natural gas to, any person or municipality engaged or legally authorized to engage in the local distribution of natural or artificial gas to the public, and for such purpose to extend its transportation facilities to communities immediately adjacent to such facilities or to territory served by such natural-gas company, if the Commission finds that no undue burden will be placed upon such natural-gas company thereby: *Provided*, That the Commission shall have no authority to compel the enlargement of transportation facilities for such purposes, or to compel such natural-gas company to establish physical connection or sell natural gas when to do so would impair its ability to render adequate service to its customers.

(b) No natural-gas company shall abandon all or any portion of its facilities subject to the jurisdiction of the Commission, or any service rendered by means of such facilities, without the permission and approval of the Com-

mission first had and obtained, after due hearing, and a finding by the Commission that the available supply of natural gas is depleted to the extent that the continuance of service is unwarranted, or that the present or future public convenience or necessity permit such abandonment.

(c) No natural-gas company or person which will be a natural-gas company upon completion of any proposed construction or extension shall engage in the transportation or sale of natural gas, subject to the jurisdiction of the Commission, or undertake the construction or extension of any facilities therefor, or acquire or operate any such facilities or extensions thereof, unless there is in force with respect to such natural-gas company a certificate of public convenience and necessity issued by the Commission authorizing such acts or operations: *Provided, however*, That if any such natural-gas company or predecessor in interest was bona fide engaged in transportation or sale of natural gas, subject to the jurisdiction of the Commission, on the effective date of this amendatory Act, over the route or routes or within the area for which application is made and has so operated since that time, the Commission shall issue such certificate without requiring further proof that public convenience and necessity will be served by such operation, and without further proceedings, if application for such certificate is made to the Commission within ninety days after the effective date of this amendatory Act. Pending the determination of any such application, the continuance of such operation shall be lawful.

In all other cases the Commission shall set the matter for hearing and shall give such reasonable notice of the hearing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by the Commission; and the application shall be decided in accordance with the

procedure provided in subsection (e) of this section and such certificate shall be issued or denied accordingly: *Provided, However*, That the Commission may issue a temporary certificate in cases of emergency, to assure maintenance of adequate service or to serve particular customers, without notice or hearing, pending the determination of an application for a certificate, and may by regulation exempt from the requirements of this section temporary acts or operations for which the issuance of a certificate will not be required in the public interest.

SECTION 8. (a) Every natural-gas company shall make, keep, and preserve for such periods, such accounts, records of cost-accounting procedures, correspondence, memoranda, papers, books, and other records as the Commission may by rules and regulations prescribe as necessary or appropriate for purposes of the administration of this act: *Provided, however*, That nothing in this act shall relieve any such natural-gas company from keeping any accounts, memoranda, or records which such natural-gas company may be required to keep by or under authority of the laws of any State. The Commission may prescribe a system of accounts to be kept by such natural-gas companies, and may classify such natural-gas companies and prescribe a system of accounts for each class. The Commission, after notice and opportunity for hearing, may determine by order the accounts in which particular outlays or receipts shall be entered, charged, or credited. The burden of proof to justify every accounting entry questioned by the Commission shall be on the person making, authorizing, or requiring such entry, and the Commission may suspend a charge or credit pending submission of satisfactory proof in support thereof.

SECTION 9. (a) The Commission may, after hearing, require natural-gas companies to

carry proper and adequate depreciation and amortization accounts in accordance with such rules, regulations, and forms of account as the Commission may prescribe. The Commission may from time to time ascertain and determine, and by order fix, the proper and adequate rates of depreciation and amortization of the several classes of property of each natural-gas company used or useful in the production, transportation, or sale of natural gas. Each natural-gas company shall conform its depreciation and amortization accounts to the rates so ascertained, determined, and fixed. No natural-gas company subject to the jurisdiction of the Commission shall charge to operating expenses any depreciation or amortization charges on classes of property other than those prescribed by the Commission, or charge with respect to any class of property a percentage of depreciation or amortization other than that prescribed therefor by the Commission. No such natural-gas company shall in any case include in any form under its operating or other expenses any depreciation, amortization, or other charge or expenditure included elsewhere as a depreciation or amortization charge or otherwise under its operating or other expenses. Nothing in this section shall limit the power of a State commission to determine in the exercise of its jurisdiction, with respect to any natural-gas company, the percentage rates of depreciation or amortization to be allowed, as to any class of property of such natural-gas company, or the composite depreciation or amortization rate, for the purpose of determining rates or charges.

SECTION 10. (a) Every natural-gas company shall file with the Commission such annual and other periodic or special reports as the Commission may by rules and regulations or order prescribe as necessary or appropriate to assist the Commission in the proper administration of this act. The Commission may pre-

scribe the manner and form in which such reports shall be made, and require from such natural-gas companies specific answers to all questions upon which the Commission may need information. The Commission may require that such reports shall include, among other things, full information as to assets and liabilities, capitalization, investment and reduction thereof, gross receipts, interest due and paid, depreciation, amortization, and other reserves, cost of facilities, cost of maintenance and operation of facilities for the production, transportation, or sale of natural gas, cost of renewal and replacement of such facilities, transportation, delivery, use, and sale of natural gas. The Commission may require any such natural-gas company to make adequate provision for currently determining such costs and other facts. Such reports shall be made under oath unless the Commission otherwise specifies.

SECTION 11. (a) In case two or more States propose to the Congress compacts dealing with the conservation, production, transportation, or distribution of natural gas it shall be the duty of the Commission to assemble pertinent information relative to the matters covered in any such proposed compact, to make public and to report to the Congress information so obtained, together with such recommendations for further legislation as may appear to be appropriate or necessary to carry out the purposes of such proposed compact and to aid in the conservation of natural-gas resources within the United States and in the orderly, equitable, and economic production, transportation, and distribution of natural gas.

SECTION 14 (b) The Commission may, after hearing, determine the adequacy or inadequacy of the gas reserves held or controlled by any natural-gas company, or by anyone on its behalf, including its owned or leased properties or royalty contracts; and may also, after hear-

ing, determine the propriety and reasonableness of the inclusion in operating expenses, capital, or surplus of all delay rentals or other forms of rental or compensation for unoperated lands and leases. For the purpose of such determinations, the Commission may require any natural-gas company to file with the Commission true copies of all its lease and royalty agreements with respect to such gas reserves.

SECTION 19. (a) Any person, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this act to which such person, State, municipality, or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. The application for rehearing shall set forth specifically the ground or grounds upon which such application is based. Upon such application the Commission shall have power to grant or deny rehearing or to abrogate or modify its order without further hearing. Unless the Commission acts upon the application for rehearing within thirty days after it is filed, such application may be deemed to have been denied. No proceeding to review any order of the Commission shall be brought by any person unless such person shall have made application to the Commission for a rehearing thereon.

(b) Any party to a proceeding under this act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set

aside in whole or in part. A copy of such petition shall forthwith be served upon any member of the Commission and thereupon the Commission shall certify and file with the court a transcript of the record upon which the order complained of was entered. Upon the filing of such transcript such court shall have exclusive jurisdiction to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 346 and 347).

(c) The filing of an application for rehearing under subsection (a) shall not, unless specifically ordered by the Commission, operate as a stay of the Commission's order. The commencement of proceedings under subsection (b) of this section shall not, unless specifically ordered by the court, operate as a stay of the Commission's order.